No. 941686 APR 14 1995

OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

SGS CONTROL SERVICES, INC.,

Petitioner,

—v.—

INTERNATIONAL ORE & FERTILIZER CORP.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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22

QUESTIONS PRESENTED FOR REVIEW

1. Whether the court of appeals abuses its discretion when, after rejecting the claim upon which the trial court's money judgment for plaintiff was based, it nevertheless affirms the judgment by substituting a different claim that had been dismissed by the trial judge and that plaintiff had waived on the appeal.

2. Whether maritime law incorporates the non-maritime law principle that where parties contract informally, an extreme disproportion between contract price and claimed damages indicates that the damages were not within the contemplation of the contracting parties.

LISTING OF PARTIES, PARENT COMPANIES AND SUBSIDIARIES

All parties to the proceeding in the court whose judgment is sought to be reviewed are named in the caption.

The parent corporation of SGS Control Services Inc. is SGS North America Inc., whose parent corporation is SGS-Societe Generale de Surveillance Holding, S.A., whose shares are publicly traded on the Swiss Bourse. SGS Control Services Inc. has two subsidiaries, Independent Cargo Services Inc. and Qualitest, S.A., neither of which is publicly traded.

TABLE OF CONTENTS

	PAGE
QUESTIONS PRESENTED FOR REVIEW	i
LISTING OF PARTIES, PARENT COMPANIES AND SUBSIDIARIES	ii
TABLE OF CONTENTS	iii
TABLE OF AUTHORITIES	iv
PRELIMINARY STATEMENT	1
The Facts of the Dispute	2
Proceedings in the District Court	3
Proceedings in the Court of Appeals	5
REASONS WHY CERTIORARI SHOULD BE GRANTED	9
Question 1: Abuse of Discretion of the Court of Appeals By Deciding Claims That Have Been Waived	9
Question 2: Disproportionality of Price to Damages Under Maritime Law	13
CONCLUSION	15

TABLE OF AUTHORITIES

Cases	PAGE
Air et Chaleur, S.A. v. Janeway, 757 F.2d 489 (2d Cir. 1985)	11
Anderson v. Branen, 27 F.3d 29 (2d Cir. 1994)	10
Arcadia, Ohio v. Ohio Power Co., 111 S. Ct. 415 (1990)	11
Boddie v. Connecticut, 401 U.S. 371 (1971)	10
Evra Corp. v. Swiss Bank Corp., 673 F.2d 951 (7th Cir.), *cert. denied*, 459 U.S. 1017 (1982)	13
Glatt v. Bank of Kirkwood Plaza, 383 N.W.2d 473 (N.D. 1986)	13
Goodstein Construction Corp. v. City of New York, 590 N.Y.S.2d 425 (N.Y. 1992)	13
Jackson v. Culinary School of Washington, 27 F.3d 573 (D.C. Cir. 1994)	9
Lebron v. National Railroad Passenger Corp., 115 S. Ct. 961 (1995)	11
Mellon Bank v. United Bank Corporation of New York, 31 F.3d 113 (2d Cir. 1994)	11
Perini Corp. v. Greate Bay Hotel & Casino, Inc., 610 A.2d 364 (N.J. 1992)	13
Rollins Environmental Services v. U.S. EPA, 937 F.2d 649 (D.C. Cir. 1991)	10
Sovereign Chemical & Petroleum Products, Inc. v. Ameropan Oil Corp., 148 F.R.D. 208 (N.D. Ill. 1992)	13

PAGE

Sundance Cruises Corp. v. American Bureau of Shipping, 7 F.3d 1077 (2d Cir. 1993), *cert. denied*, 114 S. Ct. 1399 (1994) 7

Sweet Home Chapter v. Babbitt, 30 F.3d 190 (D.C. Cir. 1994)..... 9

United States National Bank of Oregon v. Independent Insurance Agents of America, 113 S. Ct. 2173 (1993) 9

United States v. Bell, 936 F.2d 337 (7th Cir. 1991).... 10

United States v. Olano, 113 S. Ct. 1770 (1993) 10

United States v. Quiroz, 22 F.3d 489 (2d Cir. 1994)... 10

United States v. Restrepo, 986 F.2d 1462 (2d Cir. 1993)..... 10

United States v. Williams, 112 S. Ct. 1735 (1992)..... 11

Vitol Trading, S.A. v. SGS Control Services, 874 F.2d 76 (2d Cir. 1989) 7

Williams-Guice v. Board of Education of Chicago, 45 F.3d 161 (7th Cir. 1995) 9

Winston v. Children & Youth Services of Delaware Cty., 948 F.2d 1380 (3d Cir. 1991)..... 10

Statutes and Rules

12 U.S.C. § 92..... 11

28 U.S.C. § 1254 1

28 U.S.C. § 1333 1

F. R. App. P. Rule 2 11

Rule 28 12

PAGE

Rule 28(a) 11

Rule 28(b) 11

Rule 28(c) 10

Other

M. N. Kniffen, "A Newly Identified Contract Unconscionability: Unconscionability of Remedy," 63 Notre Dame L. Rev. 247 (1988) 13

Notes of Advisory Committee on Appellate Rules, Note 2 (1967) 11

Restatement of Contracts (Second), § 351(3), comment f. 13

PRELIMINARY STATEMENT

The opinion of the United States Court of Appeals for the Second Circuit, together with the dissenting opinion, is reported at 38 F.3d 1279 and is reproduced at App. A-1. The opinions of the United States District Court for the Southern District of New York are reported at 743 F. Supp. 250 and 828 F. Supp. 1098 and are reproduced at App. A-50 and A-99, respectively. The unreported opinion of the district court denying a motion for a new trial is reproduced at App. A-132.

The judgment of the court of appeals sought to be reviewed was entered on October 24, 1994. The order of the court of appeals denying the petition for rehearing was entered on January 20, 1995, and is reproduced at App. A-18. The transcript of oral argument in the Court of Appeals on April 24, 1994 is reproduced at App. A-185.

Jurisdiction to review the judgment of the court of appeals by writ of certiorari is conferred on this Court by 28 U.S.C. § 1254.

This case involves a question of federal appellate procedure and a question of maritime law, but does not involve a constitutional provision, treaty, statute, ordinance or regulation.

STATEMENT OF THE CASE

This case is within the admiralty and maritime jurisdiction of the district court pursuant to 28 U.S.C. § 1333. This case arose out of a contract between defendant SGS Control Services Inc. ("SGS") and plaintiff International Ore & Fertilizer Corp. ("Interore") for the inspection by SGS of the holds of a vessel in navigable waters in the Port of Tampa, Florida.

The inspection was performed by SGS for a contractual fee of $150. Claiming that the inspection was improperly performed, plaintiff Interore sought to recover damages of

$2,400,000. Without deciding whether the contract had been breached, the district court dismissed Interore's contract claim because the claimed damages were not contemplated by the parties. However, the district court held that SGS had negligently reported the results of the inspection and held it liable in tort for $479,687.12.

On the appeal, Interore waived the contract claim and the parties contested only the tort claim. In its decision, the court of appeals rejected the tort claim. However, the court of appeals did not reverse. Instead, with one judge dissenting, it reinstated the waived contract claim, found that the contract had been breached (despite the trial court's failure to rule on the issue of breach), and affirmed the judgment.

The Facts of the Dispute

Interore, a subsidiary of Occidental Petroleum Corp., sells phosphate fertilizer products in the international market. SGS is a surveyor of marine cargoes and vessels.

In June 1991, Interore hired SGS to sample and test a bulk cargo of phosphate and, in conjunction therewith, to inspect and report on the condition of three holds of the M/V ADELINA, prior to loading.

SGS had previously performed this type of service many times for Interore and therefore the hiring was very informal. The contract was merely a one-page telex from Interore to SGS. The telex requested that SGS inspect holds 2, 3, and 5 prior to loading, and stated in relevant part:

> Pls act our behalf performing inspection, sampling and analysis. Pls issue flwg docs: 1) Cert of hold inspection, confirming vsls holds were clean, dry and suitable.

Although not set forth in the telex, the price of the hold inspection and report, in accordance with past practice, was $50 per hold or $150 for all three.

To perform the hold inspection, SGS hired a subcontractor, Captain Luard, who had previously performed numerous hold inspections in Tampa. Captain Luard boarded the ship on July 2, 1985 and inspected holds 2, 3 and 5, and hatch covers. Luard then completed a Certificate of Readiness, which stated, in relevant part: "Said cargo compartments and HATCH COVERS have been surveyed and found suitable to load a cargo of PHOSPHATE this time and date."

After Luard completed the Certificate of Readiness, the vessel loaded the cargo and left Tampa, bound for New Zealand.

Seven months prior to the Tampa inspection, the ADELINA had carried a cargo of barley. However, since that time, the holds had been freshly painted, and Luard had not seen grains of barley that apparently were still lodged in overhead support beams. During the voyage to New Zealand, some of the grains were shaken loose and fell on top of the cargo.

When the holds were opened, a New Zealand government inspector noted what he considered to be barley contamination. Interore's New Zealand buyer, East Coast Fertilizer Co., Ltd., then refused to unload the cargo and refused to pay Interore the $2,691,803.96 purchase price. To effect salvage, Interore transported the cargo to Antwerp, where it was sold.

Proceedings in the District Court

Interore sued SGS to recover its alleged loss of $2,400,000, by filing a four-claim complaint in the United States District Court for the Southern District of New York on September 2, 1987. Interore's first three claims alleged breach of warranty under the inspection contract, negligent performance of the contract, and breach of contract. Interore's fourth claim was for tortious misrepresentation as to the condition of the holds and hatches.

After a non-jury trial on liability issues, District Judge Charles H. Tenney rendered an opinion dated August 28, 1990 and reported at 743 F. Supp. 250. Judge Tenney held that Interore could not recover compensatory damages on the contract. Although he found that the parties contemplated that SGS would use workmanlike efforts, Judge Tenney declined to reach the issues of what such efforts would entail or whether there was a breach. 743 F. Supp. at 257. Instead he found that the disproportion between the $2,400,000 of damages sought and the $150 contract price, coupled with the informal dealings between the parties, indicated that the parties had not attempted to allocate all of the risks. *Id.* at 257-258. Therefore, he ruled, the Court was justified in allocating the risks fairly. *Id.* He concluded that "[a]ccordingly," Interore should not recover compensatory damages on the contract. *Id.* at 258.

Judge Tenney also ruled that Interore's negligence claim could not be asserted because the alleged negligence was not an independent tort separate from the contract. *Id.*

However, Judge Tenney found SGS liable on the fourth claim, for negligent misrepresentation. He ruled that the Certificate of Readiness contained a negligent misrepresentation in that the inspector negligently failed to report to the vessel's representative that there were areas in the holds that he had been unable to inspect. *Id.* at 259.

Judge Tenney also found that Interore had failed to alert SGS to the extremely strict standards in New Zealand regarding importation of vegetable matter. *Id.* at 260. Ruling that Interore and SGS were equally responsible for the loss, Judge Tenney held SGS liable for 50% of the damages resulting from contamination of the Tampa cargo. *Id.*

The issues relating to damages were then tried without a jury before Chief Magistrate Judge Nina Gershon. Her report, rendered on March 31, 1993, and reproduced at 828 F.Supp. 1098, 1105, found the total damages suffered from contami-

nation of the Tampa cargo to be $959,375.44, consisting primarily of the transshipment cost from New Zealand to Antwerp and other salvage expenses. She recommended that Interore receive a damage award of $479,687.72, plus prejudgment interest.

Judge Tenney then adopted and accepted the Chief Magistrate Judge's report and recommendations, in an opinion dated August 10, 1993, reported at 828 F. Supp. 1098.

An amended judgment in favor of Interore and against SGS, in the amount of $713,666.27, inclusive of prejudgment interest, was entered on September 15, 1993.

SGS filed a notice of appeal from the amended judgment and Interore filed a notice of cross-appeal from the amended judgment.

Proceedings in the Court of Appeals

In the court of appeals, the issues and arguments presented related only to Interore's tort claim. Interore intentionally did not assert the dismissed contract claims, and thereby waived them.

SGS's appellant's brief to the court of appeals argued that liability could not be founded in tort because the dispute was governed by contract.[1] In its answering brief as appellee, Interore argued that SGS's negligent misrepresentation breached a duty independent of the contract.

The Points in Interore's Brief as to SGS's appeal were the following:

"POINT I: THE DISTRICT COURT PROPERLY RULED SGS LIABLE FOR NEGLIGENT

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[1] SGS's brief also argued that the elements of negligent misrepresentation were not established, that damages had been improperly calculated and that the trial court had committed procedural error on the issue of proximate cause.

PERFORMANCE OF PROFESSIONAL SERVICES

POINT II: JUDGE TENNEY'S FINDINGS OF FACT WITH REGARD TO SGS'S NEGLIGENCE WERE NOT CLEARLY ERRONEOUS

POINT III: THE DISTRICT COURT PROPERLY REFUSED TO OFFSET THE SETTLEMENT BETWEEN INTERORE AND EAST COAST"

[Subheadings omitted.]

These Points correspond closely to the Statement of Issues Presented for Review set forth in Interore's brief for the cross-appeal.

On its cross-appeal, Interore argued only that Judge Tenney should not have limited SGS's liability for negligent misrepresentation to 50% of the damages.

The single Point in Interore's brief as to Interore's cross-appeal was the following:

"POINT I: INTERORE WAS NOT CONTRIBUTORILY NEGLIGENT"

[Subheadings omitted.]

This Point corresponds closely to the single issue as to the cross-appeal stated in the Statement of Issues Presented for Review set forth in Interore's Brief.

Interore's brief did not state any issue, argument, reasons or citations in support of the contract claims. SGS's reply brief addressed only the issues raised by Interore and did not argue the contract claims.

At the oral argument of the appeal, Interore again declined to argue the contract claims or to argue that the contract was breached. The transcript of the argument (App. 6) confirms that Interore's counsel confined their contentions to the neg-

ligent misrepresentation claim. Midway through Interore's oral presentation, the Court asked why Interore's counsel had not cross-appealed from the dismissal of its contract claims. App. A-225. Interore's counsel answered to the effect that they thought the Second Circuit opinions in *Sundance*[2] and *Vitol*[3], as well as Judge Tenney's opinion below, were controlling. App. A-226 (*Sundance* and *Vitol* are contract cases that had disallowed consequential damages that were disproportionately large in relation to the contract prices.) Interore's counsel never disputed or distinguished these precedents, although they were presented by the panel with a clear opportunity to do so.

The court of appeals affirmed the amended judgment on October 24, 1994. The panel rejected the tort claim on which the judgment had been based. However, with one judge dissenting, the panel adopted the breach of contract claim, which Interore had already waived on the appeal, and found that the contract had in fact been breached.

Although the panel found for Interore on its waived contract claim, the panel limited Interore's recovery to the amount of the amended judgment. The panel said that "there has been no cross-appeal from the district court's dismissal of the contract claim, and we therefore leave the smaller judgment in place." 38 F.3d at 1279. Since Interore had in fact cross-appealed from the amended judgment, the finding that it failed to cross-appeal from dismissal of the contract claim could only refer to Interore's failure to argue the contract claim in its brief or at oral argument.

Interore's failure was not, however, simply a failure to cross-appeal. Interore's failure to argue or otherwise present the breach of contract claim in its brief or at oral argument

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[2] *Sundance Cruises Corp v. American Bureau of Shipping*, 7 F.3d 1077 (2d Cir. 1993), *cert. denied*, 114 S.Ct. 1399 (1994).

[3] *Vitol Trading S.A. v. SGS Control Services*, 874 F.2d 76 (2d Cir. 1989).

was also a waiver. Interore had intentionally *not* sought to sustain the judgment on contract grounds. With an eye to the opinions in *Sundance* and *Vitol*, it deliberately sought to sustain the judgment only on tort grounds. It thereby waived the breach of contract claim.

On the merits of the contract claim, the panel rejected Judge Tenney's view that the consequential damages were not recoverable due to the extreme disproportion between the fee charged and the damages claimed. 38 F.3d at 1284-1285. The panel found that the purpose of the certificate was to guarantee the condition of the hold so as to insure the preservation of the cargo. *Id.* at 1285.

Judge Tenney had also expressly not decided what specifically the contract required and had not decided whether SGS had in fact performed in a workmanlike manner. Nevertheless, and despite Interore's failure to argue these issues in the court of appeals, the court of appeals held that SGS had breached the contract. *Id.* at 1286.

The dissenting member of the panel agreed with the majority that liability could not be founded in tort. *Id.* at 1287. He too addressed the breach of contract claim, notwithstanding Interore's waiver of that claim on the appeal. *Id.* However, the dissenting judge agreed with Judge Tenney that the disproportion between the $2,400,000 of damages sought and the $150 contract price, coupled with the informality of the parties' dealings, and prior Second Circuit precedents, required dismissal of the contract claims. *Id.* at 1287-1289.

On October 7, 1994, SGS petitioned for rehearing and suggested rehearing en banc. SGS argued, *inter alia*, that it was improper for the court of appeals to decide the breach of contract claim after Interore had waived it and to find a breach when the trial judge had not reached that issue. On January 20, 1995, the court of appeals denied rehearing, without opinion.

REASONS WHY CERTIORARI SHOULD BE GRANTED

Question 1: Abuse of Discretion of the Court of Appeals By Deciding Claims That Have Been Waived

Certiorari should be granted to clarify the standard under which in civil cases a court of appeals may decide a claim that the proponent of the claim has waived. The absence of a clear standard undermines the integrity of the federal appellate process.

The Court has recognized that a court may consider an issue antecedent to and ultimately dispositive of the dispute before it, even an issue the parties fail to identify and brief in that court. *United States National Bank of Oregon v. Independent Insurance Agents of America*, 113 S. Ct. 2173, 2178 (1993).

However, the Court has not yet clearly articulated the standard for determining when the exercise of that discretion is appropriate. In the absence of a clearly expressed standard, some court of appeals' judges, relying on *Independent Insurance Agents*, assume, as the court of appeals apparently did in the present case, that they have virtually unlimited authority to decide dispositive issues, whether or not presented by the parties. *See Williams-Guice v. Board of Education of Chicago*, 45 F.3d 161 (7th Cir. 1995); *Jackson v. Culinary School of Washington*, 27 F.3d 573, 583-584 (D.C. Cir. 1994); *Sweet Home Chapter v. Babbitt*, 30 F.3d 190, 193-194 (D.C. Cir. 1994) (Silberman, J., dissenting from denial of rehearing en banc).

The court of appeals in the present case affirmed the judgment based on a claim that had not been presented and clearly had been waived. None of the judges of the panel that decided the appeal furnished any reason why deciding this waived contract claim would be a proper exercise of the court's power.

To conform to other established principles of appellate practice and to prevent a major disruption of the appellate process, the Court should set clear standards as to how the court of appeals must exercise its discretion.

The need for a standard is suggested by the requirement of due process, because limitless discretion can deprive adversely affected litigants of a meaningful opportunity to be heard. *Cf. Boddie v. Connecticut*, 401 U.S. 371, 377-378 (1971) (due process requires meaningful opportunity to be heard absent countervailing state interest of overriding significance). In this case, SGS properly relied on Interore's waiver and, in accordance with F. R. App. P. 28(c), its reply brief addressed only the arguments in Interore's answering brief. Because it followed the rules, SGS did not have a meaningful opportunity to be heard in the court of appeals on what proved to be the determinative issues in the case.

The need for a standard is also suggested by *United States v. Olano*, 113 S. Ct. 1770 (1993), where the Court carefully circumscribed the power of the court of appeals to consider issues not timely raised in the District Court in criminal cases. It would make little sense to narrowly restrict the court of appeals' power to correct plain errors at trial if at the same time the court of appeals has limitless discretion to consider unpresented issues.

The need for a standard is also suggested by the well-settled rule that failure to identify or argue an issue in a party's initial brief is a waiver of that issue and a court of appeals will ordinarily not consider that issue on the appeal, absent manifest injustice. *See, e.g., Anderson v. Branen*, 27 F.3d 29, 30 (2d Cir. 1994); *United States v. Quiroz*, 22 F.3d 489, 490 (2d Cir. 1994); *United States v. Restrepo*, 986 F.2d 1462, 1463 (2d Cir. 1993); *Winston v. Children & Youth Services of Delaware Cty.*, 948 F.2d 1380, 1385 (3d Cir. 1991); *United States v. Bell*, 936 F.2d 337, 343 (7th Cir. 1991); *Rollins Environmental Services v. U.S. EPA*, 937 F.2d 649, 653 (D.C. Cir.

1991). It is not manifest injustice to enforce a waiver resulting from the intentional tactical decision of experienced counsel. *See Mellon Bank v. United Bank Corporation of New York*, 31 F.3d 113 (2d Cir. 1994); *Air et Chaleur, S.A. v. Janeway*, 757 F.2d 489, 492 (2d Cir. 1985).

The need for a standard is also suggested by the Federal Rules of Appellate Procedure. F. R. App. P. Rules 28(a) and (b) require parties to specify and brief the issues. F. R. App. P. Rule 2, the sole rule that permits suspension of the appellate rules, authorizes the courts to relieve litigants of the consequences of default only where manifest injustice would otherwise result. *See Notes of Advisory Committee on Appellate Rules, Note 2* (1967).

The Court's recent cases are unclear as to what the standard is for the exercise of discretion to decide unargued issues. Compare *Independent Insurance Agents* and *Arcadia, Ohio v. Ohio Power Co.*, 111 S. Ct. 415 (1990) with *Lebron v. National Railroad Passenger Corp.*, 115 S. Ct. 961 (1995) or *United States v. Williams*, 112 S. Ct. 1735 (1992).

For example, judges and litigants do not now know whether the factors present in *Independent Insurance Agents* are necessary, or sufficient, for the exercise of the appellate court's discretion. In *Independent Insurance Agents*, (a) the unpresented issue (whether 12 U.S.C. § 92 had been repealed) was implicit in the respondent's argument from the start; (b) the unpresented issue involved the existence or non-existence of an Act of Congress; and (c) the court of appeals had given the parties "ample opportunity" to address the issue. *See* 113 S. Ct. at 2178-2179. In *Arcadia* the unpresented issue was implicit, and the issue involved the scope of a federal statute in relation to orders of federal agencies. In *Lebron* and *Williams*, however, while the Court recognized its power to "review an issue not pressed, but passed upon by the lower court," it failed to indicate any standard for when the reviewing court's discretion may be properly exercised.

In the present case, none of the *Independent Insurance Agent* factors appeared. The issue presented did not involve the existence (or scope) of an Act of Congress. The waived contract claim was not implicit in or antecedent to the tort claim, but rather was a separate alternative to it. SGS was not given the opportunity to address or brief the issue in the court of appeals. And, unlike *Lebron* and *Williams*, in *Interore* the court of appeals decided the dispositive issue (that the contract had been breached), even though that issue had not been passed upon by the district court.

A limitless standard for the courts of appeals *sua sponte* to review waived claims creates an immense practical problem for the appellate bar, and ultimately for the appellate courts themselves.

Absent a clear standard for when, and how, the court of appeals may consider waived issues, prudent appellants will be compelled in their *initial briefs* to raise and argue a wide range of potentially dispositive issues and claims as to which they may already have prevailed in the lower court, whether or not their adversaries wish to appeal those matters.[4] This will transform the nature—and ultimately the size—of appellants' briefs. It will also do great violence to the orderly scheme of F. R. App. P. Rule 28 which requires the appellee to raise whatever alternate issues have not been raised by the appellant and then affords the appellant the opportunity of a reply to respond to those matters.

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[4] For example, a plaintiff might prevail in the district court on the defendant's motions to dismiss based on lack of personal jurisdiction, improper venue, statute of frauds, failure to comply with a discovery order and so forth, but might lose at trial on a decisive evidentiary issue. Under *Interore*, the plaintiff-appellant's brief apparently should raise and argue not merely the evidentiary issue, but also all these pre-trial issues, whether or not defendant-appellee wishes to raise them. Otherwise, as in *Interore*, the Court of Appeals might affirm on an alternative unargued ground without the appellant's having addressed it in that court.

If the courts of appeals are to have the discretion to consider waived issues, it is vitally important to the appellate process that the Court clarify the standard under which that discretion is to be exercised.

Question 2: Disproportionality of Price To Damages Under Maritime Law

Certiorari should be granted to decide whether maritime law incorporates the principle of non-maritime contract law that where parties contract informally, an extreme disproportion between the contract price and the amount of damages claimed for breach indicates that the damages were beyond the parties' contemplation and therefore are not recoverable (the "Disproportionality Principle"). Second Circuit cases conflict on this issue and continued uncertainty significantly affects the maritime service industry.

The Disproportionality Principle is well-established in non-maritime law. *See, e.g.*, Restatement of Contracts (Second), §351(3), comment f; *Vitol Trading, S.A. v. SGS Control Services*, 874 F.2d 76, 81 (2d Cir. 1989); *Evra Corp. v. Swiss Bank Corp.*, 673 F.2d 951, 956 (7th Cir.), *cert. denied*, 459 U.S. 1017 (1982); *Goodstein Construction Corp. v. City of New York*, 590 N.Y.S.2d 425, 490 (N.Y. 1992); *Perini Corp. v. Greate Bay Hotel & Casino, Inc.*, 610 A.2d 364 (N.J. 1992) (approving the principle but finding it inapplicable to the facts); *Glatt v. Bank of Kirkwood Plaza*, 383 N.W.2d 473, 484 (N.D. 1986); M. N. Kniffen, "A Newly Identified Contract Unconscionability: Unconscionability of Remedy," 63 Notre Dame L. Rev. 247 (1988); *but see Sovereign Chemical & Petroleum Products, Inc. v. Ameropan Oil Corp.*, 148 F.R.D. 208, 213 (N.D. Ill. 1992) (declining to adopt the principle under Illinois law). The Disproportionality Principle protects contracting parties from the unduly harsh consequences of a breach where the parties have not clearly agreed to assume liability. The Disproportionality Principle recognizes the commercial reality that a very low price is a strong indication that

the contracting party did not assume a potentially crushing contingent liability for damages where the contract is informal and is silent as to such liability.

As a result of the Disproportionality Principle, commercial parties in a non-maritime context may conduct their affairs informally and inexpensively, without undue risk.

In maritime cases, however, there is a conflict within the Second Circuit as to the availability of the Disproportionality Principle. *Compare Sundance Cruises Corp. v. American Bureau of Shipping*, 7 F.3d 1077 (2d. Cir 1993) (applying the principle), *cert. denied*, 114 S. Ct. 1399 (1994), *with* the court of appeals decision in the present case.

In *Sundance*, the court of appeals applied the Disproportionality Principle, in a dispute between sophisticated commercial maritime parties, to disallow damages that were approximately 3,200 times the contract price. 7 F.3d at 1084. However in *Interore*, the court of appeals refused to apply the Disproportionality Principle even though the claimed damages were 16,000 times the contract price. *See Interore*, 38 F.3d at 1288 (dissenting opinion). Moreover, the *Interore* court suggested that it would never apply the principle in this case no matter how disproportionate ("whatever the amount") the damages claimed might be. 38 F.3d at 1285.

If the Disproportionality Principle applies under maritime law, the benefits that flow from its use in a land-based case would flow from its use in a sea-based case. If, however, under *Interore*, maritime service companies, contracting on an informal basis, are to face potentially limitless claims for liability, the effect on the maritime service industry will be dramatic. Either the cost of maritime service contracts is likely to increase markedly, or maritime service companies are likely to suffer severe financial strains. In either case, both the providers of maritime services and the consumers of those services need to know whether the Disproportionality Principle applies in maritime cases.

CONCLUSION

For the foregoing reasons, petitioner respectfully prays for issuance of a writ of certiorari to the United States of Appeals for the Second Circuit.

Dated: New York, New York
April 13, 1995

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Supreme Court, U.S.
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TABLE OF CONTENTS

1. Opinion of the Court of Appeals, dated October 24, 1994, reported at 38 F.3d 1279 . . . A-1

2. Opinion of the District Court, dated August 23, 1990, reported at 743 F. Supp. 250. . . . . A-50

3. Opinion of the District Court dated August 10, 1993, reported at 828 F. Supp. 1098 . . . . . A-99

4. Opinion of the District Court, dated October 23, 1993 (unreported). A-132

Appendix A. Report and Recommendation of the Chief Magistrate Judge, dated March 31, 1993 . . . . . A-141

5. Order of the Court of Appeals Denying Rehearing, dated January 20, 1995 (unreported). A-182

6. Transcript of Oral Argument in The Court of Appeals on April 24, 1994. . . . . A-185

1. **OPINION OF THE COURT OF APPEALS, DATED OCTOBER 24, 1994, REPORTED AT 38 F.3D 1279**

INTERNATIONAL ORE & FERTILIZER CORP.,
Plaintiff-Appellee-Cross-Appellant,
v.
SGS CONTROL SERVICES, INC.,
Defendant-Appellant-Cross-Appellee,
and
CHARLES B. UPDIKE, ESQ. and SCOTT M. RIEMER, ESQ., Appellants-Cross-Appellees.

Nos. 1480, 1481 and 1709, Dockets 93-9046, 93-9332, 94-7084

UNITED STATES COURT OF APPEALS,
SECOND CIRCUIT.

Argued April 25, 1994
Decided October 24, 1994

MICHAEL E. SCHOEMAN and CHARLES B. UPDIKE, New York City (Scott M. Riemer, Schoeman, Marsh & Updike, of counsel), for defendant-appellant-cross-appellee SGS Control Services, Inc. and appellants-cross-appellees Charles B. Updike and Scott M. Riemer.

RICHARD H. SOMMER, New York City (J. Scot Provan, Robert A. Milana, Kirlin, Campbell, Meadows & Keating, of counsel),

for plaintiff-appellee-cross-appellant.

Before: VAN GRAAFEILAND and WINTER, Circuit Judges, and MISHLER[1], District Judge.

WINTER, Circuit Judge:

SGS Control Services, Inc. ("SGS") appeals from Judge Tenney's order awarding $713,666.27 to International Ore & Fertilizer Corp. ("Interore") on the grounds that SGS negligently misrepresented the cleanliness of three ship's cargo holds resulting in contamination and other damage to the cargo. Interore cross-appeals from the district court's finding of contributory negligence and the consequent halving of damages. SGS's counsel also appeal from the

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[1] The Honorable Jacob Mishler, District Judge, United States District Court for the Eastern District of New York, sitting by designation.

district court's award of Fed. R. Civ. P. 11 sanctions for the making of repetitive motions.

We affirm but on rather different grounds. We believe that any duty that SGS owed to Interore arose from a contract between the parties to inspect the cargo holds and that SGS is not liable in tort. However, we also conclude that SGS breached its contract with Interore and that Interore would ordinarily be entitled to full damages. However, there has been no cross-appeal from the district court's dismissal of the contract claim, and we therefore leave the smaller judgment in place. We affirm the imposition of Rule 11 sanctions.

BACKGROUND

Interore, a Delaware corporation with its principal place of business in New York City is, as its name suggests, an

international corporation specializing in the trading of fertilizer products. Interore contracted to sell 22,202 metric tons of compound phosphate fertilizers to East Coast Fertilizer Company, Ltd. ("East Coast"), a New Zealand corporation, on a cost and freight basis for $4,118,287. Interore chartered the M/V ADELINA to transport the fertilizer from Sweden to Tampa, Florida, and from Tampa to Napier, New Zealand. The agreement with East Coast required Interore to have an independent hold inspector certify the condition of the holds prior to loading the fertilizer. Interore contracted with SGS, as it had several hundred times previously, to inspect the ADELINA's holds and provide such a certificate. Interore confirmed the oral contract by telex, which read in relevant part: "PLS ACT OUR BEHALF PERFORMING INSPECTION, SAMPLING AND

ANALYSIS. PLS ISSUE FLWG DOCS: 1) CERT OF HOLD INSPECTION, CONFIRMING VSLS HOLDS WERE CLEAN, DRY AND SUITABLE. . . ." Interore paid SGS $150 for the inspection of the ADELINA's three holds loaded at Tampa.

The ADELINA has five cargo holds, each approximately eighty-one by eighty-seven feet square and forty-seven feet high, separated fore and aft by vertical bulkheads. The most forward hold, hold one, is slightly narrower. On the port and starboard sides of each hold are vertical ribs protruding two feet from the side of the hull and extending from the top of the hold to where an angled section of the hold begins approximately eight feet from the floor. Horizontal bars, called stringers, are attached at regular intervals to the front of the vertical ribs, and vertical pipes are nested

between some of the ribs, each protected by horizontal bars fastened to the front of the ribs. Each hold has a large, square hatch opening at the top, measuring approximately forty-one by twenty-eight feet on hold one and fifty-five by thirty-nine feet on the other holds.

The ADELINA's previous cargo was coal, but the penultimate cargo had been barley. Although the crew cleaned and painted the holds following the discharge of the coal, they failed to remove a substantial amount of barley grains trapped in the pockets behind the stringers. The inspection of holds one and four in Sweden, performed by SGS's Swedish affiliate, lasted approximately forty-five minutes, during which the inspector descended into the holds and inspected the stringers and the hatch covers from below. The inspector also inquired of the crew as to the

vessel's prior cargoes. The inspector certified holds one and four as clean, dry, and suitable for loading.

SGS's subcontractor, Captain Peter Luard, who had four years of experience in hold inspections, performed the Tampa inspection of holds two, three, and five in the early morning hours of July 2, 1985. Between 1:45 a.m. and 2:15 a.m., Luard inspected the three holds, spending approximately ten minutes in each hold. He climbed down the aft ladders and walked the floors, inspecting the stringers and overhead deck beams. Luard did not attempt to look behind the stringers. Following his visual inspection, he was informed of the previous cargoes by the crew but did not return to the holds. At 2:15 a.m., Luard completed a document on SGS letterhead titled "Certificate of Readiness" which read:

Certificate of Readiness

THIS IS TO CERTIFY that the undersigned Marine Surveyor did, at the request of "_____" on behalf of "_____" did attend on board the *M.V. Adelina of 16356.78* Gross Tons, Port of Registry *PIRAEUS*, whereof *CAPT. MATSELOS P.* is Master and now lying at *GARDINER TERMINAL* for the purpose of surveying the following cargo holds *Nos 2, 3 and 5*. Said cargo compartments *AND HATCH COVERS* have been surveyed and found suitable to load a cargo of *PHOSPHATE* this time and date.

DATE *JULY 2nd 1985*

TIME PASSED *0215*

Peter F. Luard

for SURVEYOR

SGS CONTROL SERVICES INC.

VALID ONLY AT PORT OF ISSUANCE

Member of the SGS Group

ALL INSPECTIONS ARE CARRIED OUT TO THE

BEST OF OUR KNOWLEDGE AND ABILITY AND OUR RESPONSIBILITY IS LIMITED TO THE EXERCISE OF REASONABLE CARE [italics designate handwriting]

Following Luard's issuance of this certificate, the ADELINA loaded holds two, three and five with fertilizer and sailed for New Zealand.

Upon arrival in New Zealand on August 1, 1985, officials of the New Zealand Ministry of Agriculture and Fisheries ("MAF") discovered that the fertilizer was contaminated with barley and barred its discharge unless East Coast notified all buyers of the contamination and took steps to prevent it from being used in barley-growing areas. East Coast refused to do so or to accept the shipment, and the fertilizer remained aboard the ADELINA. Interore hired New Zealand surveyors who found the barley lodged in the stringers

and hatch covers. Following futile attempts to find other buyers in Australia or Southeast Asia, Interore shipped the fertilizer to Antwerp, Belgium, where it was sold off in small lots. During this process Interore incurred damages in costs and lost value of $ 959,375.44.

Interore brought the present action against SGS alleging breach of contract, breach of warranty, negligence, and negligent misrepresentation. In a pre-trial order, the district court bifurcated the trial into, first, a bench trial generally concerning liability issues, and, second, a hearing before Chief Magistrate Judge Gershon concerning "[a]ll issues associated with damages." The order lists the issues to be tried in the first phase as:

> whether the inspection of holds 2, 3, and 5 by SGS/Peter Luard which

resulted in the issuance by SGS Control Services of a Certificate that those holds were clean, dry and fit for the intended cargo was conducted in a proper and workmanlike manner using reasonable care and professional skill; whether SGS Control Services breached its contract with Interore to conduct a proper and workmanlike hold survey: whether SGS breached any warranties owed to Interore and whether SGS misrepresented the condition of holds 2, 3, and 5 as clean, dry and fit for the intended cargo.

Following the bench trial, the district court held that under New York law Interore could not recover on its contract claim because, "the low contract price and informal dealings between the parties indicates that they did not

attempt to allocate all the risks. Therefore, the court is justified in allocating them fairly." *International Ore & Fertilizer Corp. v. SGS Control Servs.*, 743 F. Supp. 250, 257-58 (S.D.N.Y 1990) ("*Interore I*"). In so holding, the district court relied upon the opinion in *Vitol Trading S.A. v. SGS Control Services*, 874 F.2d 76, 81 (2d Cir. 1989). The district court rejected Interore's negligence claim because SGS "did not have a duty to perform any particular kind of inspection, except as required under the contract," and, therefore, "there can be no independent tort liability for failing to take certain steps as part of that inspection." *Interore I*, 743 F. Supp. at 258. However, the district court held that SGS was liable for negligent misrepresentation for issuing the inaccurate

certification of the cleanliness and suitability of the holds, but apportioned half of the liability to Interore for its failure to inform SGS that "the slightest amount of foreign matter could contaminate the cargo" in the eyes of the vigilant New Zealand MAF. Id. at 259-60.

Following this ruling, Chief Magistrate Judge Gershon held a conference at which the parties disputed whether the district court had resolved the issue of proximate cause. Chief Magistrate Judge Gershon then referred the case back to the district court. The district court stated that Chief Magistrate Judge Gershon could "take into consideration whether the plaintiff took reasonable steps to diminish any damages," and could consider, "[i]f the plaintiff's

partial fault contributed to the damages, namely, the failure to provide a [Lloyd's Certificate of Cleanliness] document . . . ." However, the district court also cautioned SGS that any attempt to push further than these "limited" issues, "smells too much of trying to open up a trial because you forgot to do something at the time of the trial."

In her report and recommendation to the district court, Chief Magistrate Judge Gershon observed that the resolution of liability had necessarily also determined proximate cause, citing *Greyhound Exhibitgroup, Inc. v. E.L.U.L. Realty Corp.*, 973 F.2d 155, 159 (2d Cir. 1992), *cert. denied*, ____ U.S. ____, 113 S. Ct. 1049, 122 L. Ed. 2d 357 (1993). *International Ore & Fertilizer Corp. v. SGS Control Servs.*, 828 F. Supp.

1098, 1106 (S.D.N.Y 1993) ("*Interore II*"). SGS filed objections to this ruling, arguing that *Interore I* "clearly required the second phase of the trial to determine the damages *'resulting from'* the contamination of the fertilizer." (SGS's emphasis). In *Interore II*, 828 F Supp. at 1100, the district court adopted Chief Magistrate Judge Gershon's report and recommendation in full, ruling that, "the liability phase of the trial did in fact address the causation issues."

Following this ruling, SGS moved for a new trial pursuant to Fed. R. Civ. P. 59 and for amended or supplemental findings of fact pursuant to Fed. R. Civ. P. 52. SGS again argued that it had not been allowed to offer all its evidence regarding proximate causation. Interore opposed both motions and

requested sanctions pursuant to Fed. R. Civ. P. 11. The district court granted Interore's motion based on "the groundless and repetitive nature of defense counsel's motion." *International Ore & Fertilizer Corp. v. SGS Control Servs.*, No. 87 Civ. 6391 (CHT), 1993 WL 438902 at 2 S.D.N.Y. Oct. 28, 1993) ("*Interore III*"). SGS and its counsel then brought the present appeal.

DISCUSSION

We briefly summarize our holding. SGS attacks the judgment on the ground that the tort of negligent misrepresentation cannot be the basis of liability where its sole legal duties to Interore arose entirely out of a contract. This is so, SGS argues, whether resort is had to federal maritime law, *see East River S.S. Corp. v. Transamerica Delaval Inc.*, 476

U.S. 858, 90 L. Ed. 2d 865, 106 S. Ct. 2295 (1986), or to New York law, *see Clark-Fitzpatrick, Inc. v. Long Island R.R. Co.*, 70 N.Y. 2d 382, 516 N.E. 2d 190, 521 N.Y.S. 2d 653 (N.Y.1987).[2] We agree. However, we believe that Interore was entitled to recover full damages on its contract claim, which was dismissed by the district court. Interore has limited its cross-appeal to the finding that it was contributorily negligent and has thus not challenged the dismissal of its contract claim. Nevertheless, we may uphold the

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[2] On appeal, the parties dispute the proper source of law to govern our resolution of this matter. SGS argues for the application of general federal maritime law. Interore argues for the application of New York law and points out that the district court noted that both parties had assumed New York law controlled. Interore I, 743 F. Supp. at 255 n.4. Because we believe that the disposition of this case would be the same under either federal maritime or New York law, we do not address the question.

validity of a judgment on any ground, whether or not a cross-appeal has been filed. We may not, however, enlarge a money judgment absent such a cross-appeal. We therefore affirm.

1. *Breach of Contract and Negligent Misrepresentation*

[1,2] We agree with SGS that *East River*, 476 U.S. 858, 106 S. Ct. 2295, and *Clark-Fitzpatrick*, 70 N.Y. 2d 382, 516 N.E. 2d 190, 521 N.Y.S. 2d 653, compel the holding that any duty owed by SGS to Interore must be derived from the contract and that the negligent misrepresentation claim, which sounds in tort and entails a duty independent of the contract, should have been dismissed. However, we disagree with the district court that SGS was not liable for full damages for breach of contract. Under the contract, SGS was to inspect the ADELINA's holds and, if appropriate, certify that they were

"clean, dry and suitable" for the loading of phosphate. SGS was obliged by the Certificate, and by an implied duty to perform the contract in a workmanlike fashion, *see Mayer Boat Works v. Bright Marine Basin*, 265 F. Supp. 352, 355 (E.D.N.Y. 1966); *Lunn v. Silfies*, 106 Misc. 2d 41, 431 N.Y.S. 2d 282, 284 (Sup. Ct. 1980), to carry out this inspection with "reasonable care," a duty that the district court's opinion makes clear was not performed. Indeed, it is not consistent to find negligent misrepresentation on the ground that Luard "knew, or should have known, that his limited inspection did not provide a valid basis upon which to state that the hold was, in fact, free of all possible contaminants," *Interore I*, 743 F. Supp. at 259, while also holding that SGS was not liable for breach of contract for

certifying after the very same inspection that the holds were "clean, dry and suitable" for the loading of phosphate. In dismissing the contract claim, the district court relied upon *Vitol Trading S.A. v. SGS Control Services*, 874 F.2d 76 (2d Cir. 1989). However, the portion of *Vitol* relied upon represented the views of only one judge. That portion stated that SGS, the same defendant as in this case, was not liable for the full measure of damages on a contract. The portion relied upon reasoned that when a chemical tester "ha[s] no notice of potential special damages" stemming from the failure to conduct an accurate test and "as a rational economic actor . . . it would have charged substantially more for its testing services," if it knew, *Id.* at 81, SGS could not be liable for $ 500,000 in damages on a contract for which it

received only a $ 220 fee. As the other members of the Vitol panel noted in their separate opinions, these statements were dicta in which they did not join. *Id.* at 82. Moreover, that portion of the Vitol opinion cannot be reconciled with the controlling New York case *Glanzer v. Shepard*, 233 N.Y. 236, 135 N.E. 275 (N.Y. 1922), which we believe also reflects federal maritime law. In *Glanzer*, the New York Court of Appeals held independent weighers liable for special damages above the contract fee for negligent mismeasurement of commodities. The court stated that the buyers' justifiable reliance on the certificates of proper weight "was not an indirect or collateral consequence of the action of the weighers. It was a consequence which, to the weighers' knowledge, was the end and aim of the transaction." *Id.* 135 N.E. at 275.

Similarly, SGS's performance of an accurate inspection rather than a cursory one was "the end and aim of the transaction."

The fact that SGS charged a seemingly low fee relative to potential liability hardly suggests that the parties failed to contemplate SGS's bearing the risk of a negligent inspection. Indeed, the Certificate expressly "limited" SGS's "responsibility . . . to the exercise of reasonable care." SGS performs similar professional services on a frequently recurring basis and can insure against liability for inaccurate inspections which result in major damage to cargo. Then, SGS can set its prices accordingly. SGS and Interore are sophisticated repeat players in a competitive market for inspection services. We do not agree with our dissenting colleague that the parties

here had an informal arrangement that obscured from SGS the consequences of a negligent performance of its contract. SGS is a professional organization that continuously performs specialized inspections and issues formal written "Certificate[s] of Readiness" necessary to contracts of sale involving goods to be transported by sea. Interore was required by its contract with East Coast to obtain such a written certificate, and there is no significance to the fact that its request to SGS for the certificate was by phone and telex. The parties had a business relationship that involved hundreds of such transactions. There is thus no reason to treat the inspection at issue as the equivalent to a one-time-hiring of a stranger to mow one's lawn for $ 5 with resultant property damage in the thousands of dollars. SGS is a

professional organization that issues formal certificates essential to commerce that inspections have been properly done. It is fully aware that a negligent inspection may cause the loss of an entire cargo. That is why parties to sales of goods to be transported by sea require such certificates. *See generally Glanzer*. We see no reason whatsoever, therefore, why SGS is not liable for Interore's consequential damages as a result of its breach.

Our recent decision in *Sundance Cruises Corp. v. American Bureau of Shipping*, 7 F.3d 1077 (2d Cir. 1993), *cert. denied*, ____ U.S. ____, 114 S. Ct. 1399, 128 L.Ed. 2d 72(1994), is not to the contrary. Sundance was an action for damages on a contract for the classification for insurance purposes of an ocean-going passenger vessel. The court held that the

disparity between the fee charged on the contract and damages sought disclosed that the parties did not foresee the risk of such liability. However, the purpose of the contractual obligation of the ship classification society in *Sundance* contrasts markedly with that of the inspector in *Vitol* and in the present case. *Sundance* likened the suit against the classification society to a case in which "one who causes a vehicle accident . . . then sues the Motor Vehicle Bureau for damages to his car because it issued him a driver's license that falsely represented his fitness to drive. "7 F.3d at 1084. In *Sundance*, the court therefore concluded that "the purpose of the classification certificate is not to guarantee safety, but merely to permit [the ship owner] to take advantage of the insurance rates available to a classed

vessel." *Id.* The purpose of the inspection in this case, however, was precisely to guarantee the condition of the hold so as to insure the preservation of the cargo. There is no other reason to perform such an inspection and no other reason to pay for one, whatever the amount.

2. *Failure to Cross-Appeal*

[3] As noted, however, Interore failed to cross-appeal from the dismissal of its claim for breach of contract. The general rule in a case in which a party fails to cross-appeal and an appellate court would otherwise have held in its favor is that:

> [A] party who does not appeal from a final decree of the trial court cannot be heard in opposition thereto when the case is brought here by the appeal of the adverse party. In other words, the appellee may not attack the decree with a

view either to enlarging his own rights thereunder or of lessening the rights of his adversary, whether what he seeks is to correct an error or to supplement the decree with respect to a matter not dealt with below. But it is likewise settled that the appellee may, without taking a cross-appeal, urge in support of a decree any matter appearing in the record, although his argument may involve an attack upon the reasoning of the lower court or an insistence upon matter overlooked or ignored by it.

United States v. American Ry. Express Co., 265 U.S. 425, 435, 44 S. Ct. 560, 68 L. Ed. 1087 (1924). The Supreme Court elaborated on the Railway Express rule in *Morley Construction Co. v. Maryland Casualty Co.*, 300 U.S. 185, 57 S.Ct. 325, 81 L. Ed. 593 (1937), where it held that an appellee who had not cross-appealed

could not "'attack the decree with a view . . . to enlarging his own rights.'" 300 U.S. at 191, 57 S. Ct. at 328 (quoting *Railway Express*, 265 U.S. at 435, 44 S. Ct. at 564). Findings will, therefore, not be altered on a non-cross-appealing appellee's behalf "where a revision of the findings carries with it as an incident a revision of the judgment." *Id.* In short, an appellate court may not "give a new measure of relief" to the appellee. *Id.* 300 at 193, 57 S. Ct. at 328-29.

This rule has been modified in some circuits by treating the requirement of a cross-appeal as one of practice rather than jurisdiction, allowing the court to use its discretion to consider unappealed grounds so as to exercise its "broad power 'to make such disposition . . . as justice requires.'" *In re Barnett*, 124 F.2d 1005, 1009 (2d Cir. 1942) (ellipsis in original)

(citation omitted). *Compare Id. with Shipp v. General Motors Corp.*, 750 F2d 418, 428 (5th Cir. 1985) (treating cross-appeal requirement as jurisdictional); *Schildhaus v. Moe*, 319 F.2d 587, 588 (2d Cir 1963) (per curiam) (declining to review district court's findings without cross-appeal). The *Barnett* court stressed that it was sitting in equity. Generally, however, these cases have involved multiple parties where only one of several plaintiffs or defendants failed to cross-appeal. In each case, the court included the non-cross-appellant in the amended judgment so as to preserve "fairness."

Several of our recent decisions have referred without elaboration to the discretionary nature of our power to disregard the cross-appeal requirement. *Texport Oil Co. v. M/V Amolyntos*, 11 F.3d 361, 366 (2d Cir. 1993) (permitting late-

filed cross-appeal); *Finkielstain v. Seidel*, 857 F2d 893, 895 (2d Cir. 1988). These cases conform to the general rule that the appellee may seek to sustain a judgment on any grounds with support in the record. *Jaffke v. Dunham*, 352 U.S. 280, 281, 77 S. Ct. 307, 1 L. Ed. 2d 314 (1957) (per curiam) (cross-appeal not necessary to rule on admissibility of affidavit stricken by district court); *Arlinghaus v Ritenour*, 622 F.2d 629, 638 (2d Cir.) (substituting grounds for affirmance without cross-appeal), *cert. denied*, 449 U.S. 1013, 101 S. Ct. 570, 66 L.Ed. 2d 471, (1980); *Kennecott Copper Corp. v. Curtiss-Wright Corp.*, 584 F.2d 1195, 1206 (2d Cir. 1978) (observing that grant of injunctive relief may be affirmed on a claim dismissed by district court). This rule applies even when the alternate grounds were not asserted until the

court's questioning at oral argument. *Arlinghaus*, 622 F.2d at 638. We may, therefore, uphold the finding of liability on a breach of contract theory.

We do not believe, however, that, given the present procedural circumstances, Interore is entitled to its full damages. Although an appellee who has not cross-appealed may urge alternative grounds for affirmance, it may not seek to enlarge its rights under the judgment by enlarging the amount of damages or scope of equitable relief. *See, e.g., Zapico v. Bucyrus-Erie Co.*, 579 F.2d 714, 725 (2d Cir. 1978) (non-cross-appealing defendant-appellee cannot raise claim that judgments should be reduced). We may, therefore, uphold the present judgment but we may not enlarge it to award Interore its full contract damages.

Interore did cross-appeal from the

finding that it was contributorily negligent. Its sole claim in that regard is that the record does not provide a factual basis for that finding. Because we believe that SGS's liability is grounded solely in contract rather than tort, Interore's contributory negligence would be irrelevant. Arguably, we might have the power to review the finding of contributory negligence and, if we concluded that it lacked support in the record, vacate and restore to Interore the full measure of damages suffered. The restoration of the full measure, however, would be on contract grounds and thus would stretch the principles regarding cross-appeals beyond the bounds of our power.

We therefore affirm the judgment on breach of contract grounds.

3. *Rule 11 Sanctions*

[6,7] We review the imposition of sanctions under Rule 11 for abuse of discretion. *Cooler & Gell v. Hartmarx Corp.*, 496 US. 384, 405, 110 S. Ct. 2447, 2461, 110 L.Ed. 2d 359 (1990). Such an abuse would include "an erroneous view of the law or . . . a clearly erroneous assessment of the evidence." *Id.*

[8] Appellants Updike and Riemer contend that the imposition of Rule 11 sanctions violated due process because they were given neither notice nor an opportunity to be heard. *See Securities Indus. Ass'n v. Clarke*, 898 F.2d 318, 322 (2d Cir. 1990). However, they submitted an affidavit in response to Interore's opposition to SGS's motion for a new trial and supplemental findings. Interore's opposition included a request for Rule 11 sanctions. In their affidavit appellants made no mention of Interore's request for

sanctions. Appellants thus had notice from Interore's motion, and an opportunity to be heard by opposing the motion in the affidavit submitted. Appellants having failed to respond to the motion for sanctions, the district court had no reason to exercise its discretion to hold an evidentiary hearing that had not been requested.

[9] Appellants raise numerous objections on the merits to the imposition of sanctions, but, even viewing the record in the light most favorable to them, we cannot say that the district court abused its discretion. The district court had already ruled that fifty percent of the damages would be attributable to SGS because of Interore's contributory negligence. Appellants' argument that proximate cause was "associated with damages" and thus reserved for the second

phase of the trial was thus an afterthought bordering on frivolousness.

Appellants rely upon Rule 59, which governs amendment of judgments by the district court. "The major grounds justifying reconsideration" include "the need to correct a clear error or prevent manifest injustice." *Virgin Atlantic Airways v. National Mediation Bd.*, 956 F2d 1245, 1255 (2d Cir.) (citation omitted), *cert. denied*, ___ U.S. ___, 113 S. Ct. 67, 121 L. Ed. 2d 34 (1992). They claim that the district court had never clearly ruled on the proximate cause issue, and that while they acknowledge that the issue had been raised, they claim that "a formal request was necessary to raise the issue properly."

Although parties may certainly request a new trial or amended findings where

clear errors or manifest injustice threaten, in the absence of such corruption of the judicial processes, "where litigants have once battled for the court's decision, they should neither be required, nor without good reason permitted, to battle for it again." *Zdanok v. Glidden Co.*, 327 F.2d 944, 953 (2d Cir.), *cert. denied*, 377 U.S. 934, 84 S.Ct. 1338, 12 L. Ed. 2d 298 (1964). As the district court noted, SGS's arguments regarding proximate cause and related factual issues had received detailed attention at several junctures including SGS's objection to the magistrate judge's report and recommendation and in a full hearing before the district court on June 26, 1991. The district court's conclusion that SGS's motion "caused unnecessary delay to [the] proceedings and is not well grounded either in fact or in a good faith

belief in the modification of existing law," *Interore III* at 2, is therefore not an abuse of discretion.

CONCLUSION

We have examined SGS's other arguments and find them meritless. We affirm the judgment against SGS and the award of sanctions.

MISHLER, District Judge, concurring in part and dissenting in part:

I agree with the majority's ruling on the tort claim of International Ore & Fertilizer Corp. ("Interore") based on SGS Control Service's ("SGS") misrepresentation for issuing the inaccurate certification of the cleanliness and suitability of the Adelina's holds. I agree that the court may consider Interore's breach of contract claim even though Interore failed to file

a cross-appeal from the district court's dismissal of the contract claim. I also agree with the affirmance of the Rule 11 sanctions. I disagree with the majority's holding that damages of $713,666.27 (reduced by 50% on a finding of Interore's contributory negligence) is the measure of damages on the breach of contract claim.

DISCUSSION

FACT FINDINGS BY THE DISTRICT COURT

In denying recovery under Interore's breach of contract theory of liability, Judge Tenney found that the disproportion of the charge for the inspection, i.e., $150, and the damages sought;[3] and the informality at that determination. Judge Tenney found that in addition to the

> disparity between the contract price and the damages . . . the parties

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[3] Judge Tenney used the demand of $2,400,000 in the complaint.

> reach their agreement over the phone, and the plaintiff simply confirmed it with a one-page telex. The telex merely requests defendant to perform the various services and to issue a series of documents. It is devoid of any mention of liability. The low control price and informal dealings between the parties indicates that they did not attempt to allocate all of the risks. Therefore, the court is justified in allocating them fairly. Accordingly, it finds that plaintiff should not recover compensatory damages on the contract.

INTERNATIONAL ORE & FERTILIZER CORP. v. SGS CONTROL SERVS., 743 F. Supp. 250, 257-58 (S.D.N.Y. 1990) ("*Interore I*")(Drawing its analysis from Restatement (Second) of Contracts § 351 cmt. f (1979)).

The Restatement (Second) of Contracts §

351(3) (1981) notes the wide discretion that the trial court has in a breach of contract claim in limiting damages for foreseeable loss "if it concludes that in the circumstances justice so requires in order to avoid disproportionate compensation."

Comment f states:

> It is not always in the interest of justice to require the party in breach to pay damages for all of the foreseeable loss that he has caused. There are unusual instances in which it appears from the circumstances either that the parties assumed that one of them would not bear the risk of a particular loss or that, although there was no such assumption, it would be unjust to put the risk on that party. *One such circumstance is an extreme disproportion between the loss*

and the price charged by the party whose liability for that loss is in question. The fact that the price is relatively small suggests that it was not intended to cover the risk of such liability. *Another such circumstance is an informality of dealing, including the absence of a detailed written contract, which indicates that there was no careful attempt to allocate all of the risks.* The fact that the parties did not attempt to delineate with precision all of the risks justifies a court in attempting to allocate them fairly.

Restatement (Second) of Contracts § 351 cmt. f (1981) (emphasis added).

Judge Tenney made the factual finding that the damages were disproportionate to

the contract price.[4] *Interore I*, 743 F Supp. at 257. The court made this finding because the great disparity between the contract price and the damages indicated that the parties did not intend to allocate the risks.[5] Additionally, the court relied on the informality of the contract to reach its conclusion. SGS and Interore made an oral agreement that was confirmed by a one-page telex. *Interore*

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[4] This finding is not listed with the other factual findings because it was ultimately disposed of when Judge Tenney dismissed the contract claim.

[5] In *Sundance Cruises Corp. v. American Bureau of Shipping*, 799 F. Supp. 363, 376 (S.D.N.Y 1992), the district court made the same factual finding that the parties did not assume the risk of loss in making a contract in which a great disparity between the contract price and the damages resulted. The *Sundance* district court cited *Interore I* for making the same factual finding. *Id.* The Second Circuit adhered to the *Sundance* district court's factual finding. *Sundance*, 7 F.3d at 1084.

I, 743 F. Supp. at 252, 257. The agreement failed to specify the manner of inspection or mention liability. *Id.* at 257. Judge Tenney concluded that the parties did not have a "meeting of the minds" regarding the scope of the inspection and the parties did not anticipate the risk of loss. *Id.* at 256-58. These fact findings are binding on this court unless they are clearly erroneous. Fed. R. Civ. P. 52(a).

INTERPRETING SUNDANCE

Sundance Cruises Corp. v. American Bureau of Shipping, 7 F.3d 1077 (2d Cir. 1993), *cert. denied*, ___ U.S. ___, 114 S. Ct. 1399, 128 L. Ed. 2d 72 (1994) does not support the majority's analysis. The court in Sundance denied compensatory damages to Sundance, the ship owner. The court agreed with Judge Knapp's finding that "Sundance had failed to show any

damage flowing from issuance of the classification certificate." *Id.* at 1084. In other words, Sundance failed to prove causation. The court stated two additional grounds for denying compensatory damages to Sundance:

> First, the great disparity between the fee charged ($85,000) by ABS for its services and the damages sought by Sundance ($ 264,000,000) is strong evidence that such a result was not intended by the parties. We can only conclude that the small fees charged could not have been intended to cover the risk of such liability; the ship classification industry could not continue to exist under such terms. *See, e.g., Vitol Trading S.A., Inc., v. SGS Control Servs., Inc.*, 874 F2d 76, 81-82 (2d Cir. 1989) (quoting

> Restatement (Second) of Contracts § 351 cmt. f: "fact that price [charged) is relatively small suggests that it was not intended to cover the risk of such liability").
>
> Second, and probably most significantly, the shipowner, not ABS, is ultimately responsible for and in control of the activities aboard ship..... This ongoing responsibility for the vessel is supplemented by the maritime-law requirement that the shipowner has a nondelegable duty to furnish a seaworthy vessel. *Great American Ins. Co. v. Bureau Veritas*, 338 F. Supp. 999 (S.D.N. Y 1972), *aff'd*, 478 F2d 235 (2d Cir. 1973).

Id.

The reference in *Sundance* to the damages sought and the fee charged as "strong evidence that such a result was

not intended by the parties," and that the shipowner "is ultimately responsible for and in control of the activities aboard ship" indicates that the lack of causation is not the sole basis for denying damages. The *Sundance* court also cited § 351 of the Restatement which allows a court to limit damages for foreseeable loss "if it concludes that in the circumstances justice so requires in order to avoid disproportionate compensation." Restatement (Second) of Contracts § 351(3) (1981). The very fact that the *Sundance* court discussed § 351 reveals that the court extended its reasoning to cases in which causation is proven. In fact, § 351 is only applicable if the court first finds that there were damages caused by the breach. Only then would a court decide whether to limit disproportionate damages. Thus, the *Sundance* decision

supports the reasoning of *Interore I* that a court, in the interests of justice, may limit damages to avoid disproportionate compensation, if causation is proven.

The additional grounds upon which the Sundance court relied are analogous to those in *Interore I* and therefore dictate the same result. First, Judge Tenney discussed the great disparity between the contract price and the damages. Interore sought damages of $2,400,000 on a contract price of $150, a ratio of 16,000 to one.[6] *Interore I*, 743 F. Supp. at 257. The actual damages in this case were $713,666.27 compared to a contract price of $150, a ratio of 4,758 to one.

Second, the principle articulated in *Sundance* that the shipowner is ultimately responsible for the activities on a ship

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[6] Although Judge Tenney based this ratio on the pleadings, he acknowledged that the actual damages may be much lower.

is also applicable to Interore, the charterer of the Adelina. *Sundance*, 7 F.3d at 1084; *Great American Ins. Co.*, 338 F. Supp. at 1015. As the charterer, Interore was more likely than SGS to anticipate the risk of liability. Interore knew or had reason to know that the New Zealand authorities would reject the shipment if there had been minimal contamination of the fertilizer. *Interore I*, 743 F Supp. at 260. Interore was in the better position to avert the risk because it was in the fertilizer business and had shipped fertilizer to New Zealand in the past. *Id.* Even though SGS was responsible for assuring that the hold was clean, Interore could have minimized the risk of loss by advising SGS of New Zealand's strict requirements. *Id.*

I would direct dismissal of the complaint.

2. OPINION OF THE DISTRICT COURT, DATED AUGUST 23, 1990, REPORTED AT 743 F. SUPP. 250

INTERNATIONAL ORE & FERTILIZER CORP.,
Plaintiff,
v.
SGS CONTROL SERVICES,
INC., Defendant
No. 87 Civ. 6391 (CHT)
UNITED STATES DISTRICT COURT,
S.D. NEW YORK
August 23, 1990.

Kirlin, Campbell & Keating (Richard Sommer, J. Scot Provan, Robert A. Milana, Of Counsel), New York City, for plaintiff.

Schoeman, Marsh, Updike & Welt (Charles B. Updike, Scott M. Reimer, Of Counsel), New York City, for defendant.

OPINION

TENNEY, District Judge.

Plaintiff, International Ore and Fertilizer Corporation ("lnterore"), brings this breach of contract, breach of warranty, negligence and misrepresentation action against defendant, SGS Control Services, lnc. ("SGS"), alleging that SGS

improperly inspected and certified as suitable the holds of a ship hired by Interore to ship fertilizer from Tampa, Florida to New Zealand. Specifically, plaintiff contends that an SGS inspector did not perform a workmanlike inspection of the cargo holds in that he failed to observe a residue of barley in each hold. Plaintiff claims that the barley contaminated the fertilizer and ultimately caused New Zealand authorities to reject the cargo in those holds. The case was bifurcated and the liability portion was tried to the court which, for the reasons set forth below, denies recovery under the breach of contract claim but finds that defendant is fifty percent liable on the claim of negligent misrepresentation. The following, including those additional facts referred to in the Discussion, constitutes the court's findings of fact

and conclusions of law pursuant to Fed. R. Civ. P. 52(a).

FINDINGS OF FACT

Background

1. Interore is a Delaware corporation with its principal place of business in New York, New York. It is a vendor of fertilizer products in the international market. Stipulated Fact 1; *see* Tr. 3-4.

2. SGS is a New York corporation with its principal place of business in New York, New York. It provides inspection, testing and control services in connection with the movement of bulk cargoes. Stipulated Fact 2.

3. On or about May 29-30, 1985, Interore entered into a contract to sell 22,202 metric tons of compound fertilizers to East Coast Fertilizer Company Limited ("East Coast") for $4,118,287. *See* Stipulated Fact 5.

4. Interore's agreement with East Coast was on a cost and freight basis, whereby title to the product passed as soon as it was loaded on the ship and East Coast was responsible for securing its own insurance for the product. Tr. 52.

5. This was the first such arrangement that Interore had entered into with East Coast, but it had provided fertilizer to a buyer in New Zealand on one prior occasion. Tr. 50.

6. On June 7, 1985, Interore entered into a voyage charter party agreement to charter the vessel M/V ADELINA to transport the fertilizer from Landskrona, Sweden and Tampa, Florida to Napier, New Zealand. Pl. Exh. 2, Complaint ¶ 7.[7]

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[7] Under the voyage charter, the owner of the vessel had an obligation under its contract with Interore to provide a vessel with clean holds. Pl. Exh. 2 ¶¶ 2, 31. The shipowner is not a party to this action.

7. The agreement with East Coast required Interore to secure the services of a hold inspector. On June 19, 1985, Interore entered into a contract with SGS to inspect the holds of the ADELINA when it arrived in Tampa to determine whether they were suitable to load fertilizer, and also to supervise the loading, sampling, and chemical analyses of the fertilizer. Stipulated Fact 5; Tr. 11. The loading and sampling services were performed without incident and are not part of this complaint.

8. Interore had hired SGS to perform similar services 200-400 times previously. Tr. 12. As in the past, the oral agreement between plaintiff and defendant was memorialized in a telex sent by Interore to SGS, which stated in pertinent part:

Pls act our behalf performing inspection,

sampling and analysis. Pls issue flwg docs: 1) Cert of hold inspection, confirming vsls holds were clean, dry and suitable.

Pl. Exh. 19; *see* Tr. 13-14.

9. Interore paid SGS $150 (three holds at fifty dollars per hold) for the cleanliness survey, and an additional $1,859.92 for the other services. Pl. Exh. 30.

The Ship and its Prior Cargos

10. The ADELINA is a 16,356 ton bulk carrier of Greek registry built in 1977 and owned by Blue Falcon Shipping Corp. The vessel has five cargo holds. Holds two, three, four and five each measure 26.4 meters long, 24.6 meters wide, and 14.23 meters high. Hold one is slightly narrower at the front. Tr. 176; Pl. Exh. 1; Def. Exh. C, D. The holds are separated fore and aft by vertical

bulkheads. *See* Tr. 183.

11. At the aft end of each hold is an "Australian" ladder, a staircase or step ladder running at an angle rather than vertically, with hand railings and steps rather than rungs. *See* Pl. Exh. 21 (Picture 21). There is a standard vertical ladder attached to the forward bulkhead. Pl. Exh. 21 (Picture 21). The Australian ladder is accessed through a manhole cover on the deck of the ship. Tr. 180-81.

12. On the port and starboard side of each hold are vertical ribs protruding out from the hull a distance of approximately two feet. *See* Pl. Exh. 21 (Pictures 1, 22). The ribs extend from the top of the hold to about eight feet off the floor where the lower section of the hold wall runs off at a forty-five degree angle toward the floor. Tr. 237, Def. Exh. D.

The angled portion of the hold's wall covers the ship's wing tanks and measures twelve feet from the floor of the hold to the point at which it coins the side of the hull.

13. Horizontal bars, called stringers, are attached at regular intervals to the front of the vertical ribs, forming a checkerboard pattern on the port and starboard side of each hold. Pl. Exh. 21 (Picture 1); Def. Exh. D. Stringers are not commonly found in bulk carriers built today, but are quite common in older ships such as the ADELINA. Tr. 401.

14. Nested between some of the ribs are vertical pipes running along the hull from the top of the hold to the top of the wing tank. Each pipe is protected by a series of short, horizontal bars affixed to the front of the two ribs between which the pipe sits. Pl. Exh. 21 (Picture 1).

Although they extend downward only as far as the top of the wing tank, these short horizontal bars resemble and can be used as a ladder. Tr. 184-85.

15. At the top of each hold is a square hatch opening. The dimensions of the opening on hold one are 12.5m X 8.6m, and 16.7m X 12m on holds two, three, four and five. Def. Exh. C. Around the opening of the hatch, supporting the deck of the ship, are a series of deck beams. These consist of a vertical beam approximately three feet high with a horizontal lip on the lower edge, which protrudes out several inches on either side of the vertical beam. *See* Tr. 182; Pl. Exh. 20 (Picture 22).

16. On December 17, 1984, the ship carried a full cargo of barley from England to Iran. Pl. Exh. 13, 27, 28. The holds were filled to the top with the

grain. Tr. 178,254. On April 30, 1985, the vessel carried a cargo of iron ore and coal from South Africa to Rotterdam, Sweden. Pl. Exh. 13, 27, 28.

17. After the coal was discharged, the crew of the ship cleaned and painted the cargo holds. Tr. 166-67, 322-23. The cleaning was inadequate because the crew failed to remove a substantial amount of barley grains from pockets behind the stringers and the protruding lips of the deck beams. In addition, the crew painted over some of the barley that was left in the hold, although a substantial amount of barley remaining was not painted over. Pl. Exh. 20 at 3-5.

The Inspection in Landskrona

18. The ADELINA arrived in Landskrona on June 10, 1985, where it was to be loaded with 7,353 metric tons of fertilizer into holds one and four.

Stipulated Fact 3.

19. Mr. Jan Litting, an inspector from defendant's affiliate in Sweden -- SGS Skandinaviska Kontroll AB -- surveyed holds one and four. He brought with him an apprentice inspector, Mr. Ulf Svensson. Tr. 312-13.

20. Litting boarded the ship at approximately 7:00 p.m. and spoke with the first mate. He asked that the hatch cover for hold one be opened halfway. Tr. 314, 336. While this was being done, he asked the mate about the prior cargos of the ship. Tr. 332, 334.

21. He then inspected the hatch covers and proceeded to go down the Australian ladder into the hold, stopping periodically to inspect the deck beams and condition of the paint. Tr. 315-16, 339.

22. When he reached the bottom of the hold, he ordered the hatches all the way

open to see if the process of opening them caused anything to fall from the covers, which it did not. Tr. 316-17.

23. He then walked all around the tank top (floor of the hold) and looked at the stringers from below, Tr. 318, and climbed the vertical ladder to inspect them from the side, Tr. 344.

24. He and Mr. Svensson repeated this process in hold four, spending about twenty to twenty-five minutes in hold four and twenty minutes in hold one, which is smaller than hold four. Tr. 337.

25. Upon emerging from the second hold, Litting spoke with the mate again, asking him what kind of paint had been used in the holds and who had painted them. Tr. 322. He then approved the holds as clean, dry and suitable to receive the cargo. Tr. 327; Pl. Exh. 3.

26. The inspectors then went ashore

and Litting called his supervisor to report his findings, making note of the fact that the holds had been freshly painted. Tr. 325. The ship departed Landskrona on June 13, 1985, bound for Tampa. Stipulated Fact 3.

Arrival in Tampa and Mr. Luard's Inspection

27. SGS hired a subcontractor, Captain Peter Luard ("Luard"), to perform a hold cleanliness inspection in Tampa for the remaining holds. Luard had worked in the maritime industry for many years but had regularly performed hold inspections only since 1981. Tr. 267-72. In 1981 he worked for SGS in Savannah, Georgia, performing hold inspections and draft surveys exclusively for coal cargos. Tr. 273. SGS transferred him to Tampa in 1983 where he performed surveys almost entirely for ships waiting to load fertilizer. *Id.*

In late April, 1985, he left SGS to form his own company but did contract work periodically for SGS. Tr. 274.

28. The ADELINA arrived in Tampa on June 30, 1985. Stipulated Fact 4; Def. Exh. M at 1. After spending over a day at anchor, the ship picked up a pilot at 9:45 p.m. on July 1, who guided it through the harbor. Def. Exh. M at 2. At 1:20 a.m. on July 2, two tug boats were secured to the ship to bring it to the pier. *Id.* at 3. Between 1:20 and 1:45, the tugs moved the ship alongside the pier and the process of making the ship fast to the dock began. *Id.* All lines were fastened by 1:45. *Id.*

29. Luard entered the ship along with the plaintiff's representative and United States customs and immigration officials between 1:30 a.m. and 1:45 a.m. *See Id.*;

Tr. 85.[8].

30. Upon entering the ship, Luard requested that the hatch to hold five be opened, which took about five minutes. Tr. 291-92,304. Luard began to inspect the hatch cover to the first hold at approximately 1:45 a.m.

31. Luard then walked down the aft

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[8] Although the record does not indicate precisely what happened between 1:20 and 1:45, the vessel would naturally have been maneuvered to the pier by the tugs, untied from them, and then secured to the dock. It would seem virtually impossible for Luard to have been aboard the ADELINA before 1:30, as he contends is the case. On the other hand, he may well have been aboard prior to 1:45. Defendant's expert explained that a ship's gangway is frequently put down after just a few lines are tied and that the time of 1:45 a.m. on the deck log and a variety of other documents, *see* Def. Exh. M; Pl. Exhs. 15, 16, 17, reflects the time that all the lines on the boat were secured. Defendant's expert testified that it could take up to an hour to secure all the lines on a vessel the size of the ADELINA. Tr. 384. The court therefore concludes that Luard was on the ship between 1:30 and 1:45 a.m.

Australian ladder, stopping periodically for a brief inspection of the stringers and the overhead deck beams. Tr. 294-95. He proceeded to walk around the floor of the hold looking for foreign matter, and then aimed his flashlight up onto the face of the stringers and the bottom of the overhead beams. Tr. 295. He repeated this process in holds two and three. Tr. 131. At no point during his inspection did Luard attempt to look behind the stringers. Tr. 297, 303. Nor was he able to examine the upper surface of the lip of the deck beams, except to the extent that he attempted to observe the condition of the beams nearest his vantage point on the Australian ladder. Tr. 294-95.

32. He completed his inspection of the holds at 2:15 a.m., having spent approximately ten minutes in each hold. Tr. 291-92; Def. Exh. M at 3. He then

spoke to the chief mate and had a cup of coffee. Tr. 136.

33. In speaking with the mate, he learned that the prior two cargos had been barley and coal, respectively. He did not return to the holds to reinspect them for residue of either of these two materials. Tr. 137, 299-300.

34. At 2:15 a.m., Luard completed a document entitled "Certificate of Readiness." This was a standard form that had been prepared by SGS. It consisted of typewritten text and blank spaces, which Luard filled in by hand. He also supplemented the typed text, as indicated below in brackets. The completed form stated in relevant part:

Certificate of Readiness

This is to certify that the undersigned Marine Surveyor did, at the request of ____ on behalf of ____ did attend on board

the M.V./Adelina of 16,356.78 Gross Tons, Port of Registry Piraeus, whereof Capt. Matselos P is Master and now lying at Gardinier Terminal for the purpose of surveying the following cargo holds Nos. 2, 3, and 5. Said cargo compartments [and hatch covers] have been surveyed and found suitable to load a cargo of Phosphate this time and date.

DATE July 2nd 1985

TIME PASSED 0215

Peter F. Luard

SURVEYOR

for SGS CONTROL SERVICES INC.

* * * * * *

ALL INSPECTIONS ARE CARRIED OUT TO THE BEST OF OUR KNOWLEDGE AND ABILITY AND OUR RESPONSIBILITY IS LIMITED TO THE EXERCISE OF REASONABLE CARE

Pl. Exh. 14.

35. After Luard signed the

certificate, the vessel loaded 6,503 metric tons of fertilizer into hold two, 4,169 tons into hold three, and 4,175 tons into hold five. Stipulated Fact 6.

The Voyage to Napier and the Condition of the Cargo

36. The ship departed Tampa on July 4, 1985, and arrived at Napier, New Zealand on August 1, 1985. Stipulated Facts 6, 7; Def. Exh. M at 35.

37. The ship had experienced about a week and one half of rough weather on the voyage from Tampa to Napier. Tr. 223-26; Def. Exh. M at 24-34.

38. When officials of the New Zealand Ministry of Agriculture and Fisheries ("MAF") inspected the cargo in Napier, they discovered that the fertilizer in each hold was contaminated with barley. Pl. Exh. 20 at 2.

39. Later tests revealed that the

barley was infected with Tilletia Controversa (Dwarf Bunt) and Barley Stripe Mosaic Virus. *Id.* at 7.

40. The MAF officials stated that they would allow the fertilizer to be discharged only if East Coast notified all customers that the fertilizer was contaminated and that it should not be used where barley would be grown in the season following application. East Coast rejected this demand, asserting that it would injure its professional reputation as a supplier of fertilizer. *Id.* at 2; Pl. Exhs. 10, 22.

41. After MAF's initial inspection, the plaintiff hired Dominion Adjusters ("Dominion") to conduct a survey of the cargo and holds. Tr. 41. A representative of Dominion inspected the cargo and found barley lodged on the overheads, stringers and hatch covering

returns. Pl. Exh. 20 at 3, 5.

42. Most of the contaminating grains had fallen from the deck beams and hatch covering returns as evidenced by the distribution of grain in the hold. There was little or no contaminant in the "square of the hatches" (the square center of each hold directly under the hatch) but some quantity was present in the fertilizer forming the periphery of the square. *Id.* at 3; Tr. 110, 118, 191.

43. All five holds had a similar level of contamination. *Id.* at 5.

44. The MAF officials and the various parties attempted over several days to resolve the problem, but ultimately the cargo was rejected. The officials believed the barley was layered throughout the heap and therefore refused the suggestion that the crew simply pick up the visible grain ears. *Id.* at 3.

45. The photographs taken by the Dominion inspector show grain lodged behind the stringers, some of it painted over, Pl. Exh. 21 (Pictures 5-7, 11, 16 ____ 201, 24, 25, 28, 31,34, 36, 38, 41 and 42) and also scattered over the fertilizer heap, *Id.* (Pictures 2, 3, 8, 12, 17, 26, 27, 32, 33, 35, 39 and 40).

46. The cargo was ultimately resold to a buyer in Antwerp, for less than the contract price between Interore and East Coast. Tr. 49.

DISCUSSION

A. *Contract Liability*

The telex that Interore sent SGS on June 19, 1985, memorializes the agreement between the parties in this case. It requested SGS to perform a hold cleanliness inspection and to issue a certificate confirming that the holds were clean. The telex did not specify the

manner in which the inspection was to be carried out, but correspondence from SGS to Interore, like the Certificate of Readiness prepared by Mr. Luard, provides: "All inspections are carried out to the best of our knowledge and ability and our responsibility is limited to the exercise of reasonable care." Pl. Exhs. 4, 5, 6 and 14. Considering the long history between the parties, that degree of care was incorporated in this contract as well.[9] The parties did not define

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[9] Therefore, it is unnecessary to determine whether defendant was also bound by any implied warranty to provide reasonable care. *See Great American Insurance Co. v. Bureau Veritas*, 338 F. Supp. 999, 1013-15 (S.D.N.Y. 1972), *aff'd*, 478 F.2d 235 (2d Cir. 1973); *Ryan Stevedoring Co. v. Pan-Atlantic S.S. Corp.*, 350 U.S. 124, 133-34, 76 S. Ct. 232, 100 L. Ed. 133 (1956); Note, *Liability of Marine Surveyors for Loss of Surveyed Vessels: When Someone Other than the Captain Goes Down with the Ship*, 64 Notre Dame L.Rev. 246, 261-70 (1989); *McCormack, Warranties and Disclaimers*, 62 Tul.L.Rev. 549, 560-68 (1988).

"reasonable care," but when a contract for services requiring special skills does not contain a provision describing how the service is to be rendered, New York law requires the service be performed in a "workmanlike manner."[10] *Vitol Trading S.A., Inc. v. SGS Control Services, Inc.*, 680 F. Supp. 559, 567 (S.D.N.Y. 1987), *rev'd on other grounds*, 874 F.2d 76 (2d Cir. 1989); *Lunn v. Silfies*, 106 Misc. 2d 41, 44, 431 N.Y.S. 2d 282, 284 (Sup. Ct. 1980).

Generally speaking, how the service is customarily performed in the industry will be strong evidence of what is reasonable or workmanlike. *See* W. Keelon, D. Dobbs, R. Keeton, D. Owen, *Prosser and Keeton on Torts* § 33 at 194-95 (5th ed. 1984) [hereinafter *Prosser*]. The parties

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[10] Both parties have assumed that New York law controls.

dispute what the standard in the industry is concerning inspection of the stringers and the overhead beams, the areas where the grain was found. Defendant's expert, Captain Shore ("Shore") and plaintiff's expert, Captain Davenport ("Davenport") agreed that a reasonable inspector, when entering the hold, would stop periodically on the access ladder to direct the beam of a flashlight onto the stringers and deck beams, Tr. 186, 316, and would inspect them again from the tank top. Tr. 186-87, 318, 400. Shore testified that inspectors would thereafter climb the forward vertical ladder to the top of the hold, again stopping periodically to inspect the stringers and deck beams visually. Tr. 186-87. Luard's inspection was substantially similar to the hypothetical

survey described by Shore.[11]

Davenport testified that an inspector should take additional measures to check behind the stringers. Specifically, Davenport testified that when he performs an inspection on a vessel with stringers, he runs up the wing tanks and then climbs the pipe guards, looking for contaminant in the pockets formed by the stringers and the vertical ribs. Tr. 238. Shore testified that he does not run up the wing tanks and knows of no inspector who does. Tr. 380, 391. He added that he had once attempted to run up the wing tank of a

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[11] Although the evidence suggests that Luard did not climb the forward vertical ladder, and spent only ten minutes in each hold, see Findings of Fact 2933, the court will assume for the 'purposes of this discussion that Luard performed an inspection as thorough as that described by Shore. This is because the Swedish inspector substantially performed such an inspection, see Findings of Fact 20-25, but nevertheless failed to detect the grain.

ship in doing a structural survey, but was unable to do so. Tr. 404. Luard and the Swedish inspector also testified that it was not standard practice to run up the surface of the wing tanks. Tr. 144, 282, 351.

The parties apparently did not have a "meeting of the minds" on precisely what the inspection would entail. Considering their past relationship, each contemplated that the defendant would exercise reasonable care, which obligated it to use workmanlike efforts. In determining what steps this would actually require, plaintiff maintains that the court should interpret "workmanlike conduct" by an objective standard of reasonableness. which would require the surveyor to perform an inspection reasonably calculated to find hidden contaminants. Plaintiff asserts that the surveyor should

either climb the wing tanks as Davenport does, or get a ladder from the crew to enable him to inspect behind the stringers. Plaintiff contends that Shore's inspection would be adequate in a modern ship built without stringers, but is inadequate and, therefore unworkmanlike in a ship with stringers. *See Prosser* § 33 at 194 ("[C]ustoms which are entirely reasonable under the ordinary circumstances which give rise to them in the first instance may become entirely unreasonable in the light of a single fact altering the situation in the particular case.") Plaintiff argues that if the industry standard is as defendant's expert describes, it is deficient. Plaintiff cites *The T.J. Hooper*, 60 E.2d 737, 740 (2d Cir. 1932) (Hand, J.) for the proposition that because an entire industry may be negligent, industry custom

is only some evidence of what is reasonable: the court must ultimately decide whether the service in question was performed negligently.

Defendant argues first that Davenport's testimony is not credible, claiming it is virtually impossible to run up the wing tanks and climb the pipe guards. Although it may be a difficult procedure in some types of holds, it is certainly not an impossible task, especially in a hold whose wing tanks are shorter and flatter than others. *See* Tr. 238. Even if it could be done, however, SGS claims that the parties contracted only for the standard industry inspection, which did not involve any more extensive checking of the stringers than that carried out by Mr. Luard. *See Vitol*, 680 F. Supp. at 567; *Milau Assoc., Inc. v. North Ave. Dev. Corp.*, 42 N.Y. 2d 482, 486, 368 N.E.2d

1247, 1250, 398 N.Y.S.2d 882, 885 (1977) ("[R]easonable care and competence owed generally by practitioners in the particular trade or profession defines the limits of an injured party's justifiable demands."). Indeed, SGS claims that its inspectors have performed inspections without checking behind the stringers on many prior occasions. Noting that contract law allows the parties to agree on whatever type of inspection they choose, SGS argues that the interpretation of the parties' intent regarding the term "reasonable" should be limited by the custom and practices in the industry.

Although contract law provides a method to resolve such disputes over interpretation, *see, e.g.*, A. Corbin, *Corbin on Contracts* § 536 (1960 & Supp. 1990), the court need not reach the issue of what "workmanlike efforts" would

entail. Whether it does, or should, involve efforts as extensive as that suggested by plaintiff or could be satisfied by the inspection performed by Luard, would not be determinative because even if Luard violated his contractual duties, SGS would not be required to pay the full amount of damages plaintiff seeks. The mere fact that one party to an agreement has failed to satisfy a contractual duty of care does not necessarily mean that it will be held fully liable for all resulting damages, even if foreseeable.

It is not always in the interest of justice to require the party in breach to pay damages for all of the foreseeable loss that he has caused. There are unusual instances in which it appears from the circumstances either that the parties assumed that one of them would not bear

the risk of a particular loss or that, although there was no such assumption, it would be unjust to put the risk on that party. One such circumstance is an extreme disproportion between the loss and the price charged by the party whose liability for that loss is in question. The fact that the price is relatively small suggests that it was not intended to cover the risk of such liability. Another such circumstance is an informality of dealing, including the absence of a detailed written contract, which indicates that there was no careful attempt to allocate all of the risks. The fact that the parties did not attempt to delineate with precision all of the risks justifies a court in attempting to allocate them fairly.

Restatement (Second) of Contracts § 351 comment f (1979). Interore paid SGS fifty

dollars per hold or one hundred fifty dollars to perform the cleanliness inspection in Tampa, and seeks damages of $2,400,000. In a case very similar to the one at bar involving the same defendant, *Vitol Trading S.A., Inc. v. SGS Control Services*, 874 F.2d 76, 81 (2d Cir. 1989), plaintiff sought damages in the amount of $547,688 on a contract price of $220, a ratio of approximately 2,500 to one. The Second Circuit explained that if SGS intended to assume so great a risk, it would have charged substantially more for its services. Alternatively, it would have turned down the plaintiff's offer, rather than risk so much for so little.

In this case, the disparity between the contract price and the damages is even greater. Plaintiff seeks damages of $2,400,000 on a contract price of $150, a

ratio of 16,000 to one.[12] *See Evra Corp v. Swiss Bank Corp.*, 673 F.2d 951, 956 (7th Cir.) (difference between damages of $2,100,000 too disproportionate to contract price of $27,000), *cert. denied*, 459 U.S. 1017, 103 S. Ct. 377, 74 L. Ed. 2d 511 (1982); cf. *Kenford Co. v. County of Erie*, 108 A.D.2d 132, 137 n. 5, 489 N.Y.S.2d 939, 944 n. 5 (App. Div. 1985) (damages not out of proportion to profit defendants could have made), *aff'd*, 67 N.Y.2d 257, 493 N.E.2d 234, 502 N.Y S.2d 131 (1986). In addition, the parties reached their agreement over the phone, and plaintiff simply confirmed it with a one-page telex. The telex merely requests

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[12]Admittedly this ratio is based on the pleadings; the actual damages may be much lower. Nevertheless, considering that plaintiff will recover fifty-percent under its tort cause of action, the court need not decide how much, if any, it could also recover under a contract theory.

defendant to perform the various services and to issue a series of documents. It is devoid of any mention of liability. The low contract price and informal dealings between the parties indicates that they did not attempt to allocate all of the risks. Therefore, the court is justified in allocating them fairly. Accordingly, it finds that plaintiff should not recover compensatory damages on the contract.[13]

B. *Tort Liability*

The court's denial of recovery under the contract theory is based upon the disparity between the contract price and

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[13] As explained in the following discussion, defendant's erroneous statement that the holds were clean permits plaintiff to recover under the tort theory of negligent representation. Because the court has held that plaintiff cannot recover under the contract theory, it does not decide whether this incorrect certification also violated any implied warranty that the statements in the "Certificate of Readiness" would be accurate.

the damages incurred. Nevertheless, that consideration does not apply to the analysis of defendant's duties under independent tort law.

When the duty of one person to another exists solely by virtue of a negotiated agreement, the relationship is normally governed only by the law of contract. *See Niagara Mohawk Power Corp. v. Stone & Webster Engineering Corp.*, 725 F. Supp. 656, 662 (N.D.N.Y. 1989); *Carmania Corp., N.V. v. Hambrecht Terrell Int'l*, 705 F. Supp. 936, 938 (S.D.N.Y. 1989). Accordingly, a violation of that duty does not ordinarily give rise to a remedy in ton. *Niagara*, 725 F. Supp. at 661-62. Nevertheless, if the conduct of one party would constitute a ton in the absence of the contract, then that cause of action is not extinguished simply because some aspects of the relationship between the

parties happen also to be governed by an independent agreement. *Id.*: *Eaves Brooks Costume Co., Inc. v. Y.B.H. Realty Corp.*, 76 N.Y.2d 220, 556 N.E.2d 1093, 557 N.Y.S.2d 286 (1990) (plaintiff may properly bring an action in ton when defendant had assumed a duty to exercise reasonable care 10 prevent foreseeable harm to plaintiff).

Plaintiff has urged two theories under ton law, negligence and negligent representation. Plaintiff's negligence claim asserts that defendant unreasonably failed to detect the presence of the contaminating barley. Essentially, plaintiff argues that defendant had a duty to perform a "reasonable" inspection, which would have at least involved inspecting the stringers on the sides of the hold. Unfortunately, the duty to inspect the hold arose only by virtue of

the contract. For example, without the contract, there would have been no duty requiring defendant to send a representative to inspect plaintiff's ship. Similarly, defendant did not have a duty to perform any particular kind of inspection, except as required under the contract. Indeed, nothing in the law of tort would have imposed additional duties on defendant if the parties had agreed that the surveyor was supposed to conduct only a limited inspection. Since the duty to inspect arose only by virtue of the contract, which was freely negotiated by the parties, there can be no independent tort liability for failing to take certain steps as part of that inspection. *See Niagara* at 662; *Clark-Fitzpatrick, Inc. v. Longlsland R.R. Co.*, 70 N.Y.2d 382, 389, 516 N.E.2d 190, 193-94, 521 N.Y.S.2d 653, 656-67 (1987).

That does not rule out liability for negligent misrepresentation, however. Under the law of negligent misrepresentation, a person will be held liable for damages arising from the reliance by another on a representation that the person knows, or should have known, was not true. *See White v. Guarente*, 43 N.Y.2d 356, 353, 372 N.E.2d 315, 319, 401 N.Y.S.2d 474, 478 (1977); *Ultramares Corp. v. Touche*, 255 N.Y. 170, 181-82, 174 N.E. 441, 445 (1931). In addition, "[a] representation made with an honest belief in its truth may still be negligent, because of lack of reasonable care in ascertaining the facts." *Prosser* § 107 at 745. The agreement called for Luard, after finishing his inspection, to provide a document confirming that he had performed an inspection and found the holds to be suitable to receive the cargo.

As previously noted, the parties probably did not have a meeting of the minds as to exactly how, or how extensively, Luard would inspect the holds. They each knew, however, that Luard's inspection was to be the last check before the fertilizer was loaded. Moreover, Luard had the authority to block the loading if he were not satisfied with the condition of the hold. In fact, all of the inspectors including Luard have on occasion delayed the loading of a cargo so that crews could properly clean the holds. *See* Tr. 283-84,349, 408-09.

Therefore, defendant must have realized that if it provided the certificate, plaintiff would take no further steps to determine the state of cleanliness of the holds. Even if, as defendant argues, it had no duty under contract or ton law to do more than was the practice in the

industry, it must have been aware that in entering into this agreement, plaintiff was relying, if not on the actual inspection itself, then at least on this document for reassurance that the fertilizer could safely be loaded.

Luard should also have known that his representation about the cleanliness of the holds might have been inaccurate. He testified that he looked at the stringers only from the vantage point of the Australian ladder. Considering the orientation of the stringers and their distance from these ladders, the court is skeptical that Luard could have adequately observed whether they were clean. Even if he could see those portions of the stringers close to the ladders, he should have known that this would not necessarily be indicative of the portions further away. For example, just like Luard, a

cleaning crew would have difficulty reaching the center section of the stringers, although it could more easily access the areas by the ladders. *See* Tr. 300. As a matter of common sense, Luard should have realized that the cleanliness of easily accessed areas would not necessarily reflect the condition of those that were difficult to reach.

Both plaintiff's and defendant's experts, as well as Luard, testified that the back of the stringers is an area where one would expect to find cargo residue. Tr. 17879, 192, 298,401. Therefore, Luard knew, or should have known, that his limited inspection did not provide a valid basis upon which to state that the hold was, in fact, free of all possible contaminants. Accordingly, he should not have simply signed a certificate that reasonably led plaintiff to assume it was

clean.

Instead, Luard should have reported to Mr. Clemente Colon, plaintiff's representative on the ship, that there were areas in the hold that he could not inspect in the course of his routine survey.[14] Colon had the ultimate responsibility for deciding whether the cargo would be loaded. Armed with this information, Colon could have intelligently decided how to proceed. *See* Tr. 74, 93. For example, he might have decided that a further delay was warranted and asked defendant to secure a ladder to check the stringers. Shore testified that

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[14] This does not mean that an inspector in Luard's position, must actually meet with the plaintiff's representative. It would have been equally acceptable if the Certificate of Inspection had clearly stated that only those areas actually inspected were found to be clean, and had included a section noting the areas that the inspector was not able to examine.

it is normal to request a ladder whenever an inspector wishes to see an area that cannot otherwise be accessed. Tr. 408-09. Indeed, in this case, if Luard had told Colon that he could not attest to the cleanliness of the hold, Colon would likely have requested a ladder and this loss would have been avoided. Even in the case of a vessel with overhead beams and no stringers, the plaintiff's representative could take further investigatory steps such as inquiring of the cleaning crew how the beams were cleaned, if at all.[15] Since the risk of

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[15] If the situation were warranted, the seller's representative might even take extraordinary measures such as lowering a crew member down from the hatch opening to inspect the beams. Although such action was certainly not contemplated to be pan of defendant's inspection, the failure to alert Colon to the possibility of contamination prevented him making a reasoned judgment as to what steps should be taken to help determine how to proceed.

an incorrect decision to load might result in a loss of several million dollars, it would seem likely that Colon would have wanted to take whatever additional steps were reasonable under the circumstances to protect the cargo.[16]

Although Luard was negligent in failing to inform plaintiff that there remained a risk of contamination, part of the reason for his failure was because plaintiff had not brought home to him the risks involved. Tort law attempts, *inter alia*, to put the risk of loss on the party best able to avert it. *See Prosser* § 4.

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[16] The court does not address the more difficult situation in which defendant can prove that the plaintiff's representative would not have taken additional steps after learning of the potential risk. Nor does it address those situations in which the inspector himself has taken every reasonable step to determine whether the hold was clean, leaving nothing for the plaintiff's representative to do.

Interore was in the fertilizer business and had previously shipped fertilizer to New Zealand. In fact, Interore sent a representative to New Zealand specifically to handle this contract. Tr. 4, 31. The inspector from Dominion notes in his report that the New Zealand officials are extremely strict regarding the importation of foreign vegetable matter. Pl. Exh. 20 at 8. Since it was in the fertilizer business and had dealings with New Zealand authorities before, plaintiff was in a better position than defendant to know that even minimal contamination of grain could result in rejection by the New Zealand authorities. If it did not know, it should have known because a reasonable seller of fertilizer would have determined the requirements for bringing its product into a foreign country.

When it retained defendant's services,

plaintiff could easily have alerted it to the strict standards of cleanliness that were necessary. Had Luard been informed that the slightest amount of foreign matter could contaminate the cargo, he would likely have performed a more thorough inspection. That does not diminish Luard's negligence for representing that the hold was clean, but it illustrates that each party had exclusive knowledge of facts that, if communicated to the other, might well have avoided the risk of loss. The court therefore finds that the plaintiff and defendant are equally responsible for the barley not being discovered and apportions fault at fifty percent each.

CONCLUSION

Defendant is liable for fifty percent of the damages resulting from contamination of the fertilizer. The

actual amount of damages will be determined in the second phase of the trial.

So ordered.

3. **OPINION OF THE DISTRICT COURT, DATED AUGUST 10, 1993, REPORTED AT 828 F. SUPP. 1098**

INTERNATIONAL ORE & FERTILIZER CORP., Plaintiff,

v.

SGS CONTROL SERVICES, INC., Defendant.

No. 87 Civ. 6391 (CHT)

United States District Court, S.D. New York

August 10, 1993.

OPINION and ORDER

TENNEY, District Judge:

In 1987, plaintiff International Ore and Fertilizer Corp. ("Interore") brought an action for breach of contract, breach of warranty, negligence, and misrepresentation against SGS Control Services, Inc. ("SGS"). In 1985, Interore contracted to sell fertilizer to East Coast Fertilizer Co., Ltd. ("East Coast"). Three of the holds of the M/V ADELINA were used to ship the fertilizer from Tampa, Florida to New Zealand;

Interore hired SGS to inspect the holds before the fertilizer was stored.

Although SGS had certified the holds as clean, upon arrival in New Zealand the fertilizer was found to be contaminated with the remains of barley previously stored in the holds. The Ministry of Agriculture and Fisheries ("MAF") refused to allow the fertilizer in the country, and East Coast refused to accept it, except at a significantly reduced price. Interore ultimately shipped the fertilizer to Antwerp and sold it there. This suit followed.

The case was bifurcated and the liability portion was tried before this court. *International Ore & Fertilizer Corp. v. SGS Control Services, Inc.*, 743 F. Supp. 250 (S.D.N.Y. 1990). This court held that compensatory damages were not allowed, that SGS could not be held liable

on the theory of negligent inspection of the holds where the duty arose solely by virtue of contract, and that SGS would be held 50% liable on the theory of negligent misrepresentation for approving the holds as suitable without alerting Interore that there were areas of the ship's holds that SGS was not able to inspect. Interore was found to share in the blame, because it failed to notify SGS's inspector of the strict standard of cleanliness required because of both the nature of the cargo and New Zealand's standards regarding the importation of foreign vegetable matter. Familiarity with the prior opinion is assumed.

A three day trial on the damages portion of this case was then heard before Chief Magistrate Judge Nina Gershon. She issued a report and recommendation on March 31, 1993 (the "Report"), which is

attached as Appendix A. Pursuant to 28 U.S.C. § 636(b)(1) and Federal Rule of Civil Procedure 72(b), the parties were given ten days to submit written objections to the report. By order of this court dated April 12, the time was extended. Both parties submitted timely objections. For the reasons stated below in discussing various objections raised, this court now accepts and adopts all the recommendations in the Report.

I. *Objections to Evidence Heard and Magistrate Judge's Findings*

SGS has objected on a number of grounds that go to the narrowing of issues by the magistrate judge at the damages phase. In all respects, however, the magistrate judge acted properly.[17]

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[17] The court finds it difficult to separate several of SGS's objections that stem from the same root: SGS has to pay costs that it believes are disproportionate to its degree of fault, and it objects that it has been held

A. Presentation of Proximate Cause Issue

SGS broadly objects that the magistrate judge prevented it from defending on the basis that its conduct was not the proximate cause of the contamination of the fertilizer. SGS claims that this court's opinion "clearly required the second phase of the trial to determine the damages 'resulting from' the contamination of the fertilizer." Defendant's Objections to Report ("Def. Obj."), at 15. SGS interprets this to imply that

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liable for damages resulting from the contamination. However, this court held previously that SGS would share fault equally with Interore, and its liability was clearly established on the basis of negligent mis-representation. Thus, the magistrate judge was not at liberty to reconsider liability issues, but to calculate damages. She properly declined to hear again the objections that SGS had to this court's previous opinion. While each objection will be addressed and ruled upon separately, see Fed. R. Civ. P. 72(b), those that address issues already ruled upon by this court will not be extensively discussed.

proximate cause was an issue for determination in the damages phase. SGS proposes either that a hearing now be held specifically for the purpose of litigating the proximate cause issue, or that Interore's damages be significantly reduced.

While objections to specific monetary figures will be addressed below, it should be noted at the outset that the liability phase of the trial did in fact address the causation issues. As the magistrate judge explained, there can be no liability without proximate cause being established. *See* Report at 2; 743 F. Supp. at 259. Implicit in any finding of overall negligence is the idea that causation -- one element of negligence -- has been established. *See Greyhound Exhibitgroup, Inc. v. E.L.U.L. Realty Corp.*, 973 F.2d 155, 159 (2d Cir. 1992), *cert. denied*, ___

U.S. ___, 113 S. Ct. 1049, 122 L. Ed. 2d 357 (1993); *see also* infra part II.A.

B. Frederick Phillips's Testimony and Economic Conditions

Along similar lines, SGS continues to press its claim that the damages sought by Interore were not caused by the contamination, but rather by poor economic conditions in New Zealand and the MAF's allegedly shocking rejection of the fertilizer. SGS claims that it was barred from presenting evidence at the hearing that would have established this causation.

The magistrate judge heard testimony from SGS's own witness, Frederick Phillips, who testified as to market conditions in New Zealand at the time of delivery. While the magistrate judge found that Phillips's testimony "supported the difficulties in salvaging the cargo in New Zealand," Report at 6, she found that

SGS's attempt to tie East Coast's refusal to buy the fertilizer to market conditions, rather than the contamination, was "supported only by speculation." *Id.*

The fact that the magistrate judge did not find this testimony convincing obviously does not provide grounds for a retrial or a hearing. SGS did not present testimony from anyone at East Coast to establish a causal link. Upon a review of the record, this court agrees that the evidence presented did not tie East Coast's rejection to market and economic conditions.

SGS also objects that Phillips's testimony was not given the appropriate weight by the magistrate judge. She stated that his testimony did not prove specifically any other reasons that East Coast might have rejected the shipment.

Although Phillips was a member of the

MAF, he did not handle any of the events concerning the ADELINA. He did not perform any testing on the barley seeds, he only knew of the MAF's test results on the barley "by hearsay," and his only involvement with the purchase of fertilizer in New Zealand came from buying small amounts for samples. Transcript ("Tr. "), dated 3/11/92, at 111-14.[18]

Interore's attorney asked Phillips whether he had any personal knowledge "as to why East Coast refused to buy the cargo [in 1985]?" Phillips responded: "I have some opinions. I have -- no. I could draw a scenario but it's not my job to do that. No, I have no personal knowledge." Tr., dated 3/11/92, at 143. Given that Phillips did not have any such knowledge

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[18] Because the transcript of the trial before the magistrate judge is not consecutively paginated, references are noted by the page within the transcript and the date of the hearing.

(or if he did, SGS's attorneys did not elicit it during the trial), it follows logically that his testimony on this point was speculative and therefore unpersuasive -- to both the magistrate judge and this court.

C. David Ritchie's Testimony and Barley Contamination

SGS claims that the magistrate judge "made an implicit finding that the sound fertilizer could not be segregated from the barley." Def. Obj. at 43. It asserts that this conclusion was erroneous, and that in coming to it the magistrate judge relied too heavily upon the testimony of Interore's expert witness, David Ritchie.

First, SGS's incorrect reading of the report should be pointed out. Upon its arrival in Antwerp, the fertilizer was separated into two categories: "heavily damaged" or "admixed with barley," and

"said to be sound."[19] The magistrate judge stated:

> The term "said to be sound" rather than "sound" was used because, by virtue of the nature of the cargo and the *possible* layering of the contaminant, no one was prepared to guarantee that the "said to be sound" cargo was in fact sound. Nonetheless, Interore was able to sell the fertilizer, in various lots, at a substantial price.

Report at 7-8 (emphasis added). It would require a creative reading to find that this statement implicitly finds that the barley was layered throughout the cargo. The relevance of the statement is

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[19] SGS argues that the term "heavily damaged" was never used, but that the more heavily contaminated fertilizer was labelled "admixed with barley." In either case, this category contained the fertilizer in which barley was visible.

that MAF officials in New Zealand *believed* that barley was mixed in; this court made such a finding previously, *see* 743 F. Supp. at 255 (Finding of Fact 44), and SGS cannot mischaracterize the report to object to that finding now.

SGS also objects that the magistrate judge "relied heavily" on Ritchie's testimony: "Central to [Chief Magistrate] Judge Gershon's determination that Interore mitigated its damages was her finding that [SGS] did not establish that the barley could have been removed from the fertilizer and that this would have been less costly than the method Interore chose." Def. Obj. at 41.

SGS makes much of the fact that Ritchie is now a member of the Board of Directors of the successor to East Coast. It is not at all apparent to this court that the magistrate judge "relied heavily" on

Ritchie's testimony. Her discussion relating Ritchie's understanding did no more than this court's opinion had done previously -- find that the MAF believed that the barley was layered throughout the fertilizer.

II. Objections to Calculations

A. Interore's Mitigation Costs

SGS argues that the factors leading to Interore's shipping to Antwerp were not ones for which they should be responsible, because they were not damages "resulting from" the contamination of 3.7% of the cargo.

SGS has long contended that New Zealand's particularly strict standards concerning contaminated cargo made the cargo difficult to sell in that country. However, this argument -- as stated in the Report -- was accounted for by this court's apportioning of damages equally

between the two parties. *See* Report at 8 (citing *Interore*, 743 F. Supp. at 260). The court found fault with Interore in part because of its failure to inform SGS of these standards.

Furthermore, SGS has failed to recognize the primary reason that Interore's mitigation costs were assessed against it and added into the final formula of damages. While this court did rule that SGS was not to be held responsible for unforeseeable damages, it did not provide that SGS should not be held responsible for *mitigation costs*. The costs that Interore expended en route to Antwerp were not unforeseeable consequential damages, but costs of mitigation -- the costs of salvage that are properly deducted from the fair market value formula.

It is reasonably foreseeable that a

negligent misrepresentation could lead to rejection of cargo, and that salvage may reasonably only be obtainable in other ports. *See* Report at 3. That this specific event might transpire need not be reasonably foreseeable; rather, the general type of harm must be. *See Parsons v. Honeywell, Inc.*, 929 F. 2d 901, 905-06 (2d Cir. 1991) ("'foreseeability includes the probability of the occurrence of a general type of risk involving the loss, rather than the probability of the occurrence of the precise chain of events preceding the loss .... "' (quoting *Tucci v. Bossert*, 53 A.D.2d 291, 293, 385 N.Y.S.2d 328, 331 (2d Dep't 1976))).

B. *Incorrect Formula Used for Calculations*

SGS has raised a number of objections broadly complaining that the report "does not reach a logical or equitable result." Def. Obj. at 13. SGS bases this argument

primarily on the fact that the invoice value of the Tampa cargo minus the gross sales proceeds shows that the value of the cargo was diminished by a maximum of $91,675.96. Yet such a calculation totally ignores the costs of mitigation that Interore incurred -- sales expenses and salvage. It seems obvious to this court (as it did to the magistrate judge) that these mitigation costs are to be factored in when calculating damages based upon differences in market value. *See Ostano Commerzanstalt v. Telewide Systems, Inc.*, 684 F. Supp. 1172, 1176 (S.D.N.Y. 1988), *modified, 880 F.2d 642 (2d Cir. 1989)*. While the cost of salvage was high, the ocean shipment of the goods was necessary.

C. Incorrect Application of Formula

SGS also claims that damages were incorrectly calculated, even assuming that the magistrate judge applied the correct

formula. It argues that damages "should only include reduction in the value of that portion of the fertilizer which could not be segregated from visible barley, the extra unloading costs incurred in making the separation, and the demurrage costs in New Zealand incurred when the MAF delayed the unloading of the ship." Def. Obj. at 24. According to SGS, these damages total $47,413.27. Upon review of the record, it does not appear that SGS ever proposed this particular breakdown of damages calculation in the past. Nor is it a sound proposal: it purports to sever the damages to only apply mitigation costs to the contaminated fertilizer, when Interore was forced to move the entire shipment to Antwerp.

D. Weight Loss of Tampa Cargo

Interore objects that the magistrate judge awarded SGS a "weight loss" credit.

The contaminated cargo was found to be short by a certain weight when it was off-loaded at Antwerp. The pro rata value of this shortage was $39,533. The magistrate judge credited this sum to SGS because "when and how the weight loss occurred is not clear from the record. . . . While [SGS] is properly charged with reasonable salvage expenses. . . it is not properly charged with damage to the cargo not attributable to its conduct." Report at 16.

According to Interore, "[t]he evidence clearly indicates, as well as common sense, that the weight loss occurred during [the] salvage process due to the necessity for repeated handling." Plaintiff's Objections to Report at 6. Consequently, Interore argues, the cost is one that SGS should bear.

The magistrate judge did not accept

this argument. This court agrees upon a review of the record that Interore failed to prove that the weight loss must have occurred during salvage. The burden was on Interore to establish where the loss occurred; they have failed to show even that the salvage process, and the "necessity for repeated handling," customarily causes any kind of weight shortage. The magistrate judge appropriately awarded SGS a credit for the weight loss.

E. Interore's Address Commission

Interore objects that in arriving at the total of the salvage costs, the magistrate judge did not account for the "address commission" paid by Interore of $9,874. 16.[20] She stated that Interore

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[20] This amount is actually the pro rata share apportioned to the cargo at issue; the total address commission was $14,764.

could not recover the amount as part of its "ocean freight" charges, because it actually did not pay the money as freight, but retained it. The issue was discussed at length at the hearing with Interore's witness, Michael Hefferen. He testified that the payment -- which totalled $14,764 -- was called an address commission, but was in fact applied toward the purchase of liability insurance for the ocean voyage.

Interore claims that the money was an insurance premium, ultimately paid out by it "through an internal memo credit-debt system," Obj. at 8, even though there was not a specific accounting of the figure. However, Hefferen testified on direct examination that Interore retained the $14,764. Tr., dated 3/10/92, at 29. When asked by the court during cross-examination to clarify whether the address commission went back to Interore's parent

company, Occidental Petroleum ("Occidental"), the following exchange occurred:

THE COURT: May I just clarify something because I think the question earlier was, whether or not the address commission goes back to the parent [Occidental]?

HEFFEREN: No, it does not.

THE COURT: I thought you said essentially it does?

HEFFEREN: No, it does not. It never goes back to the parent.

THE COURT: That stays in your pocket?

HEFFEREN: That's correct. We get charged for charterer's liability insurance at the end of the year. It is figured in some way with Frank B. Hall and Occidental Petroleum and whatever it comes out to be, we get charged for it accordingly.

Id. at 48. When attempting earlier to

describe the work done by Hall, who apparently was the insurance broker for both Interore and Occidental, Hefferen had stated: "I honestly don't know all the ramifications and how Frank B. Hall figures out the cost of the charterer's liability insurance. I honestly don't know." *Id.* at 47.

It appears from testimony that Interore retained the address commission. However, even if a payment was ultimately made that accounted for the money Interore claims here, Interore failed to prove at trial that any such amount was owed; Hefferen's testimony was inconclusive. Under these circumstances, SGS is not required to pay the commission.

F. Pre-Judgment Interest

1. SGS's objection

SGS argues that Interore is not entitled to any prejudgment interest,

because "special circumstances" exist here, namely that both parties were at fault. Def. Obj. at 46. Pre-judgment interest customarily is allowed in maritime tort cases, and should be granted absent exceptional circumstances. *See Mitsui & Co. v. American Export Lines, Inc.*, 636 F.2d 807, 823 (2d Cir. 1981).

SGS refers to cases that have limited pre-judgment interest because of "a mutual fault collision in which both parties are damaged." *Iberian Tankers Co. v. Gates Constr. Corp.*, 504 F.2d 747, 747 (2d Cir. 1974); *see also Afran Transport Co. v. The Bergechief,* 285 F.2d 119 (2d Cir. 1960). These cases base their reasoning upon *The Wright,* 109 F.2d 699 (2d Cir. 1940). As Judge Clark explained in that case, admiralty cases in which both parties are at fault, and both parties are damaged, often create an exceptional circumstance.

"This is based on the uncertainty as to the party which will have the ultimate liability to make payment on determination of the balance due." *Id. at 702*. That is, where two vessels are damaged and there is mutual fault, it is not clear until ascertained by the court which party is owed the greater amount of damages.

In this case, there was mutual fault but injury only to one party, and the damages were ascertainable from the outset.[21] These are not the special

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[21] Because damages were easily ascertainable, SGS cannot successfully argue that Interore's damages claim was so excessive that it precluded meaningful settlement negotiations, creating a special circumstance. It may be the case where damages are speculative that a defendant expects a plaintiff's demand to be reduced during negotiation, and that an excessive claim precludes such meaningful negotiations. Here, the damages claimed were high, but they were easily ascertainable. Moreover, SGS cannot argue that the damages are excessive relative to the contract price. Such an argument is precluded because SGS was held liable not based on the contract, but based on a

circumstances contemplated by the cases that SGS cites, and this court is not persuaded that the policy behind *The Wright* should be extended.

2. Interore's Objection

In her report, the magistrate judge directed the Clerk of the Court to use the interest rates paid each month on 52-week United States Treasury bills during the applicable period in calculating pre-judgment interest. Interore complains that the magistrate judge had indicated at trial that she would apply the statutory rate, which under New York law is 9%. Other than a brief discussion in the record, the issue was not discussed or briefed. *See* Tr., dated 3/18/92, at 247-48.

However, in its pre-trial memorandum of

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theory of negligent misrepresentation. See supra note 1.

law, Interore relied on the precedent of *Ingersoll Milling Machine Co. v. M/V BODENA*, 829 F.2d 293 (2nd Cir. 1987), *cert. denied*, 484 U.S. 1042, 108 S. Ct. 774, 98 L. Ed. 2d 860, (1988) for the proposition that the interest rate used in awarding pre-judgment interest rests within the trial court's discretion. Interore claimed that this allowed the court "to tailor the rate of interest to the particular circumstances of the case in order to achieve the purpose of making the injured party whole." Plaintiff's Memorandum of Law in Support of Damages, Submitted March 28, 1991, at 12. Interore made no reference to New York statutory rates or to state law.

In her report, the magistrate judge relied on the broad discretion afforded courts in determining the rate of pre-judgment interest, tying

the interest in this case to Treasury bill rates. *See Ingersoll*, 829 F.2d at 311 (because of fluctuations in Treasury bill rates over the relevant period, the district court did not abuse its discretion in applying a rate based on an average for pre-judgment interest); *Independent Bulk Transp., Inc. v. Vessel "MORANIA ABACO"*, 676 F.2d 23, 25-27 (2d Cir. 1982) (plaintiff in admiralty action is entitled to income that monetary damages would have earned, which ought to be measured by interest on short-term, risk-free obligations). She then adopted the Treasury bill formula, because of the fluctuations in interest rates over the long period of time covering the pre-judgment period, citing *In re Potomac Transport, Inc.*, Nos. 82 Civ.

0805 (JFK), 83 Civ. 4597 (JFK), 1993 U.S. Dist. LEXIS 418, 1993 WL 17206 (S.D.N.Y. Jan. 19, 1993). In that case, the court vacated a judgment prepared by the Clerk of the Court that set the pre-judgment interest rate in an admiralty action at 9%, in compliance with N.Y. Civ. Prac. L. & R. § 5004 (McKinney 1992). Concluding that "federal law applies in admiralty actions," the court employed the "short-term, risk free obligations" logic of *Independent Bulk Transp.*, and tied the pre-judgment interest rates to one-year Treasury bills.

This court agrees with the recommendation in the Report. The magistrate judge indicated from the bench that she thought New York law would provide the applicable pre-judgment

interest rate, as it provided the underpinnings of negligent misrepresentation, which was the initial basis of liability. Tr., dated 3/18/92, at 247-48. However, in the Report, she correctly relied on precedent applying federal law to admiralty actions.

The court is not required to apply a New York statute setting interest in a case based solely on admiralty jurisdiction, with no assertion of diversity jurisdiction. Indeed, the plaintiff points to no admiralty case in which the New York statute has been applied to pre-judgment interest. The court therefore exercises its discretion and adopts the formula for pre-judgment interest suggested in the Report, finding it to be in full agreement with the precedent and practice of this circuit and the principles of federal admiralty

jurisdiction.

G. Settlement Credit

SGS has also claimed that the Report improperly failed to apportion the proceeds of the settlement that has already taken place between Interore and East Coast.[22] However, the settlement provides that East Coast will pay Interore, through its underwriter, $400,000 in connection with other cargo -- not including the fertilizer -- on the ship. SGS did not offer any evidence at the trial of the damages portion of this case to indicate that the settlement agreement should not be accepted on its face. As a rule, the court should look to such an agreement on its face to determine the intent of the settling panics. *See*

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[22] Although SGS's objection in this regard consists of one sentence, see Def. Obj. at 47, nonetheless it must be addressed. See Fed. R. Civ. P. 72(b).

Hess Oil Virgin Islands Corp. v. UOP, Inc., 861 F.2d 1197, 1208 (10th Cir. 1988). Yet SGS made no showing that there was intent contrary to that made plain in the settlement agreement. Because the agreement did not cover damages to the Tampa cargo, it should not be taken into account.

Conclusion

For the above stated reasons, the report of Chief Magistrate Judge Gershon is adopted in full. Consequently, Interore is entitled to receive from SGS $479,687.72 in accordance with the Report, and pre-judgment interest is to be calculated according to the interest rates paid each month on 52-week United States Treasury bills during the relevant period. Furthermore, in accordance with Federal Rule of Civil Procedure 58, the court orders the Clerk of the Court to prepare a

final judgment in accordance with this opinion.

SO ORDERED.

4. **OPINION OF THE DISTRICT COURT, DATED OCTOBER 23, 1993 (UNREPORTED)**

INTERNATIONAL ORE & FERTILIZER CORP, Plaintiff, v. SGS CONTROL SERVICES, INC., Defendant.
INTERNATIONAL ORE & FERTILIZER CORP v. SGS CONTROL SERVS. 87 Civ. 6391 (CHT)

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK 1993 U.S. Dist. LEXIS 15198

October 28, 1993, Decided

October 28, 1993, Filed

OPINION AND ORDER

TENNEY, District Judge,

This action arises out of an admiralty claim brought by International Ore and Fertilizer Corp. ("Interore") against SGS Control Services, Inc. ("SGS"). *See International Ore & Fertilizer Corp. v. SGS Control Serv., Inc.*, (S.D.N.Y., Aug. 10, 1993) (No. 87 Civ. 6391) ("Interore II"); *International Ore & Fertilizer Corp. v SGS Control Serv., Inc.*, 743 F. Supp. 250 (S.D.N.Y. 1990) ("Interore I"). SGS moves the court for a new trial under Fed. R.

Civ. P. 59 and for amended or supplemental findings of fact under Fed. R. Civ. P. 52. Interore opposes the motion and requests sanctions against defense counsel pursuant to Fed. R. Civ. P. 11. The court denies SGS's motion, and imposes sanctions against the law firm of Schoeman, Marsh & Updike to reimburse plaintiff for attorney's fees and costs incurred in responding to this groundless and frivolous motion.

SGS moves for a new trial on the issue of proximate causation. SGS argues that it has not had the opportunity to argue the issue of proximate causation before this court. Memorandum of Law in Support of Motion to Amend Findings and for a New Trial at 4; Affidavit of Charles Updike in Support of Motion for New Trial at 7-8. This court and a magistrate judge have specifically addressed the issue of proximate causation in this matter on

several occasions. *See Interore II*, at 4-5, 9-10; *Interore I*, 743 F. Supp. at 260; Report of Chief Magistrate Judge Gershon, Mar. 31, 1993 at 2. Interore I established that Interore and SGS shared blame for the loss of value to the cargo. *Interore I*, 743 F. Supp. at 260. As we noted in our opinion in Interore II, proximate cause was properly addressed at the liability phase of the trial, not at the later damages phase of the trial. *Interore II*, at 5; *see, Greyhound Exhibitgroup, Inc. v. E.L.U.L. Realty Corp.*, 973 F.2d 155, 159 (2d Cir. 1992), *cert. denied*, 122 L. Ed. 2d 357, 113 S. Ct. 1049 (1993). SGS has failed to establish any persuasive reason consistent with Fed. R. Civ. P. 59 for the court to reopen this previously addressed issue. Simple disagreement with the court's findings does not constitute grounds for a

new trial. *Geshwind v. Garrick*, 738 F. Supp. 792, 793 (S.D.N.Y 1990).

SGS also asks this court to amend its earlier findings of fact. Specifically, SGS challenges the court's finding that the New Zealand Ministry of Agriculture and Fisheries ("MAF") refused to allow the fertilizer into New Zealand. According to SGS, this finding is unsupported by the record, directly contradicts the evidence, and is clearly erroneous. Updike Aff. PP 3-5. The court begs to differ.

Abundant evidence supports the fact that the MAF prevented unloading of the cargo for its intended purpose. Defendant's own exhibits demonstrate unambiguously that the MAF refused the shipment in its original condition. *See* Exhibit 22. SGS's own prior pleadings concede that the MAF "prohibited discharge until the grain was examined and declared

free of contamination" and that the MAF eventually only "permitted the fertilizer to be discharged subject to removal and destruction of the visible barley grain." Defendant's Pre-Trial Memorandum of Law in Opposition to Plaintiff's Claim for Damages at 6. April 19, 1991: see Objections of SGS to Magistrate's Report at 11.

The court believes sanctions appropriate due to the groundless and repetitive nature of defense counsel's motion. The court's 1990 opinion in Interore I held that SGS was liable for 50% of the damages. Interore I limited the second phase of the trial to a determination of the actual amount of damages, and was not intended to permit relitigation of the elements of the liability claim. See Interore I, 743 F. Supp. at 260. Almost continually during

this action, defense counsel has argued that it has not received an adequate opportunity to address the proximate cause issue. In fact, this court held a full hearing two years ago on whether the issue of proximate causation had received sufficient attention. *See* Transcript of Hearing, June 26, 1991. The court concluded that there was no need to reopen the question of proximate causation, but that SGS would be permitted to introduce evidence of Interore's mitigation of damages before the magistrate judge. The parties then introduced evidence relating to mitigation of damages before the magistrate judge, which should have been the end of the issue. *See* Magistrate Judge's Report and Recommendation at 4-9. Receiving an unfavorable ruling on the mitigation issue, defense counsel once again attempts to raise the issue under

the guise of proximate causation.

Counsel has raised this issue at every possible juncture of this case. SGS's current motion is substantively identical to several previous motions, most recently its Objections to the Magistrate's Report, filed May 24, 1993. Sanctions serve as deterrence and punishment for reasserting arguments that have been rejected unambiguously and repeatedly by the court. *See Vekris v. Peoples Express Airlines, Inc.*, 707 F. Supp. 679, 682 (S.D.N.Y. 1988). Defense counsel has crossed the line between zealous representation and frivolousness. The court finds that SGS's current motion has caused unnecessary delay to these proceedings and is not well grounded either in fact or in a good faith belief in the modification of existing law. Where, as here, counsel repeats its earlier arguments without introducing new

evidence, and fails to support its allegations of manifest errors of law or fact, the court does not believe that plaintiff should bear the costs of responding to the motion. *See Sassower v. Field*, 138 F.R.D. 369, 375-77 (S.D.N.Y. 1991), *aff'd in relevant part*, 973 F.2d 75 (2d Cir. 1992), *cert. denied*, 113 S. Ct. 1879 (1993); *Vekris*, 707 F. Supp. at 682.

Plaintiff to submit an affidavit of reasonable costs and attorney's fees within 20 days of entry of this order.

SO ORDERED.

APPENDIX A. REPORT AND RECOMMENDATION OF THE CHIEF MAGISTRATE JUDGE, DATED MARCH 31, 1993

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

INTERNATIONAL ORE & FERTILIZER CORP.,
Plaintiff,

-against-

SGS CONTROL SERVICES, INC.,
Defendant.

March 31, 1993, Decided

REPORT AND RECOMMENDATION

87 Civ. 6391 (CHT)

GERSHON, Chief Magistrate Judge:

The Honorable Charles H. Tenney, District Judge, following a non-jury trial, has found defendant SGS Control Services, Inc. ("SGS") liable to plaintiff International Ore and Fertilizer Corporation ("Interore") for negligent representation. 743 F. Supp. 250 (S.D.N.Y. 1990). In 1985, Interore entered into a contract to sell fertilizer to East Coast Fertilizer Company Limited ("East

Coast"). The fertilizer was loaded in Landskona, Sweden and in Tampa, Florida and transported on the M/V Adelina, which Interore chartered. This suit involves only the Tampa cargo, which was carried in three holds of the vessel.

SGS issued a certificate of cleanliness as to the holds of the M/V Adelina. The holds in fact were not free of barley (which had been transported from England on a prior carriage). In the case of fertilizer, barley is a contaminant. Judge Tenney found that SGS's inspector "knew, or should have known, that his limited inspection did not provide a valid basis upon which to state that the hold was, in fact, free of all possible contaminants. Accordingly, he should not have simply signed a certificate that reasonably led plaintiff to assume it was clean." 743 F. Supp. at 259. Judge Tenney further found

that plaintiff shared the blame, in that it failed to notify SGS's inspector of the strict standards of cleanliness required; plaintiff, Judge Tenney found, knew or should have known that even the slightest amount of foreign matter could contaminate the cargo and cause rejection by the New Zealand authorities, who impose extremely strict standards on the importation of foreign vegetable matter. *Id.* at 260. For that reason, SGS was held liable only for fifty percent of "the damages resulting from contamination of the fertilizer." *Id.* Trial of the actual amount of the damages sustained was referred to me. This Report constitutes my findings of fact and conclusions of law under Rule 52 of the Federal Rules of Civil Procedure.

Before turning to the facts, certain preliminary legal issues will be addressed. First, Judge Tenney's

post-trial finding of liability established that SGS's negligent representation proximately caused Interore to be damaged. "With regard to liability, the concept of proximate cause supplies the legal nexus between act and injury, and provides a necessary basis for awarding compensation." *Greyhound Exhibitgroup, Inc. v. E.L.U.L. Realty Corp.*, 973 F.2d 155, 159 (2d Cir. 1992), *cert. denied*, 122 L. Ed. 2d 357, 113 S. Ct. 1049 (1993). SGS now seeks to argue that its negligence was not the proximate cause of Interore's loss. Its arguments go to "the legal nexus between act and injury." They should have been presented, if at all, at the liability phase of the trial.

SGS also argues that the damages sought were not reasonably foreseeable. As Judge Tenney has already noted (and as I find

would be obvious to anyone in the industry, including SGS), "the risk of an incorrect decision to load might result in a loss of several million dollars...." 743 F. Supp. at 259. Clearly, a negligent representation that a hold is clean could lead to contamination of the cargo to be stowed in the hold. It is also foreseeable that, if a cargo is rejected because of contamination, it may become necessary to salvage it by selling it to other parties and, further, that it may be necessary to ship it elsewhere to obtain a reasonable salvage price, as happened here.

SGS correctly notes that plaintiff is not entitled to consequential damages flowing from a breach by its buyer, East Coast, of its contract with Interore. SGS argues that the damages Interore should be awarded should be no greater than those

Interore could obtain from a carrier who failed to comply with its obligations of carriage, generally, the difference between the fair market value of the cargo at destination in the condition in which it should have arrived and the fair market value in the condition in which it did arrive, less salvage. *See Kanematsu-Gosho Ltd. v. M/T Messiniaki Aigli*, 814 F.2d 115, 118 (2d Cir. 1987): *Encyclopedia Britannica, Inc. v. S.S. Hong Kong Producer*, 422 F.2d 7, 18 (2d Cir. 1969), *cert. denied*, 397 U.S. 964 (1970). In effect, this is what plaintiff seeks. It takes as its starting point the invoice value of the Tampa cargo, and deducts from that its gross salvage recovery, reduced by its sales expenses and other expenses of mitigation.

Plaintiff of course has the obligation to mitigate its damages, but "the burden

of shoving that a plaintiff unreasonably failed to minimize damages rests with the wrongdoer." *Federal Ins. Co. v. Sabine Towing & Transportation Co., Inc.*, 783 F.2d 347, 350 (2d Cir. 1986): *accord Sutton River Services, Inc. v. Inland Tugs Co.* 1985 A.M.C. 858, 862 (S.D. Ill. 1984). Moreover, plaintiff was required only to act reasonably to minimize its damages. It was not required to take extraordinary measures to mitigate nor even measures which, in hindsight, might have been more successful. *See, e.g., Federal Ins. Co., 783 F.2d at 350; Ellerman Lines, Ltd. v. The President Harding*, 288 F.2d 288, 289-91 (2d Cir. 1961). Plaintiff is entitled to recover "costs incurred in reasonable attempts to mitigate damages." *Ostano Commerzanstalt v. Telewide Systems, Inc.*, 684 F. Supp. 1172, 1176 (S.D.N.Y. 1988), *modified*, 880 F.2d 642 (2d Cir.

1989).

On arrival of the vessel at Napier, New Zealand on August 1, 1985, the New Zealand Ministry of Agriculture and Fisheries ("MAF") found the fertilizer to be contaminated with barley. On the same day, Interore's buyer, East Coast, refused to take delivery of the fertilizer. David W. Ritchie, a New Zealand farmer and chairman of New Zealand's Federated Farmers, which exercised great control over the entry of farm products into the country, testified, wholly credibly, as both an expert in New Zealand farming activities and from personal knowledge of the reaction of New Zealand's farmers to the arrival of the vessel bearing contaminated fertilizer on New Zealand's shores. In 1985, Ritchie had been the chairman of the Agricultural Section of the Federated Farmers. There was concern

both that the barley was diseased and that, even undiseased, the barley would lead to contamination of barley seed production and the downgrading of New Zealand's malting barley crop.

At the end of August, the MAF cleared the cargo for landing in New Zealand, in the following language: "The barley in and with the fertilizer cargo in the M.V. Adelina at Napier may be introduced subject to all visible barley being removed and destroyed under supervision of an inspector before the cargo of the fertilizer is discharged." This did not change Ritchie's view or that of the Federated Farmers that the cargo should not be landed. It was Mr. Ritchie's understanding at the time that the barley could not be separated out from the fertilizer. According to Mr. Ritchie, the fertilizer could not be salvaged except at

a substantial discount. (He noted that under similar circumstances a later cargo of fertilizer had been destroyed.) In his view, its sole use was for pastoral farming, that is, for animal grazing purposes and, since pastoral farmers generally do not purchase high analysis fertilizer which this was, the price would have to have been substantially discounted.

William J. Hueston, who in 1985 was a senior vice-president of plaintiff in charge of trading, described Interore's efforts to mitigate its damages. After the MAF released the cargo for landing in New Zealand, Interore attempted to renegotiate the price with East Coast, but East Coast offered only an unacceptably low salvage price of less than 50%. Interore then sought other potential buyers in New Zealand and Australia but

received no offers to purchase the cargo.

Frederick Phillips, a New Zealand economist and government employee, called by SGS, who was not a farmer and had no personal involvement in the events, described the economic climate in New Zealand in 1985. His testimony supported the difficulties in salvaging the cargo in New Zealand. He speculated as to other, market reasons why East Coast may have rejected the fertilizer, but no such reasons were proved. In sum, SGS's argument that the unwillingness of either of the two main buyers of fertilizer in New Zealand, East Coast and Ravenswood, to offer a substantial price for the fertilizer was the result of fluctuations in the currency exchange rate and a drop in demand rather than the reduction in value of the cargo as the result of contamination is supported only by

speculation.

SGS's argument that Interore was unreasonable in not dispatching someone to assist John Hayes, its sales representative in New Zealand, in the effort to sell the cargo in New Zealand is not supported by the evidence. Hayes was in telephonic communication with headquarters. The failure of Interore to locate a buyer in New Zealand was not the result of an unreasonable failure on the part of Interore to have physically sent someone else to New Zealand.

When the cargo could not be sold in New Zealand, potential buyers in Australia and Southeast Asian countries were approached, but this effort also was unsuccessful. Interore also considered discharging the fertilizer and warehousing it for a short time for sale in lots to buyers in New Zealand or Southeast Asia, but it

concluded that this would not be cost effective.

Ultimately, Interore transported the fertilizer on the M/V Adelina to Antwerp, where it had a major marketing staff, where storage facilities were readily available, where there was a market for each of the fertilizer blends contained in the shipment and where it could be sold in smaller quantities to maximize the price obtained. Also, the barley was of English origin (*see* 743 F. Supp. at 252) and apparently of less concern in the European market. The M/V Adelina sailed from Napier on September 27, 1985 and arrived at Antwerp on November 9, 1985.

Alex Etien, Interore's senior shipping and traffic manager, operating from Interore's headquarters in Belgium, had the responsibility to arrange for the discharge operation in Antwerp. He

organized a survey at which all interested parties, including SGS, were represented. Water damage was discovered in Hold No. 5 of the ship.

During discharge, the cargo was divided into two categories, heavily damaged (by barley contamination) and "said to be sound." The term "said to be sound" rather than "sound" was used because, by virtue of the nature of the cargo and the possible layering of the contaminant, no one was prepared to guarantee that the "said to be sound" cargo was in fact sound. Nonetheless, Interore was able to sell the fertilizer, in various lots, at a substantial price.

REASONABLENESS OF MITIGATION.

Applying the standard of mitigation set forth above to the facts, I satisfied that Interore acted reasonably in its efforts to mitigate its damages. The

circumstances it faced were unusual, but it acted with reasonable expedition and efficacy to reduce its injury.

SGS makes much of the fact that the refusal of East Coast to accept the cargo at an adjusted price was contrary to prior experience. But East Coast did ultimately agree to accept the cargo at a reduced price; the problem was that the reduced price was so low that it made economic sense for Interore to transport the fertilizer to Antwerp, with the attendant shipping and other costs, rather than to accept East Coast's proposal. SGS has not disputed that Interore's damages are less because of its decision not to accept East Coast's reduced price. Moreover, the extent to which the unusually strict nature of New Zealand's attitude toward the importation of even minimally contaminated foreign vegetable matter may

have enhanced the damages, in that it affected East Coast's response to the cargo and the response of the other potential New Zealand buyer, forcing plaintiff to seek more distant buyers, is accounted for in Judge Tenney's determination to apportion the damages equally between SGS and Interore. *See* 743 F. Supp. at 260.

The reliance by SGS on *M. Golodetz Export Corp. v. S/S Lake Anja*, 751 F.2d 1103, 1112 (2d Cir.), *cert. denied*, 471 U.S. 1117, 86 L. Ed. 2d 261, 105 S. Ct. 2361 (1985), is misplaced. There, the goods at destination, though nonconforming, were marketable, but plaintiff allowed the goods to sit and, by their nature, lose value, for eighteen months while it tried to force acceptance through arbitration, rather than attempting to mitigate through third-party

sales. Here, in contrast, Interore spent a reasonable time attempting to clear the goods for landing at Napier and convince its buyer to accept them, but then moved to obtain other buyers.

SGS also argues that it would have been easy to remove the barley, and presumably make it acceptable in the New Zealand market, but the evidence does not establish that the effort needed to accomplish this would ultimately have been less costly, and have led to less damage to plaintiff, than the method Interore chose. While ultimately Interore was quite successful in selling the fertilizer in Europe, a "substantial amount of barley grains" were in the cargo holds, 743 F. Supp. at 252, a surveyor at Napier found "barley lodged on the overheads, stringers [horizontal bars extending down the sides of the holds] and hatch covering returns,"

Id. at 255, and it was "believed the barley was layered throughout the heap. . . . " *Id.* Moreover, in addition to the cost of removing the barley, plaintiff would have had other expenses, including the expenses of discharge and warehousing, and it had no assurance that the fertilizer would be sold in Napier. It cannot be said that Interore's decision to transport the fertilizer to Antwerp was unreasonable.

VALUE OF GOODS AT DESTINATION.

Interore reasonably takes as its starting point in determining damages the invoice value of the Tampa cargo, $2,691,003.96. In the absence of non-speculative, persuasive evidence that the invoice value did not fairly reflect the fair market value of the cargo in the condition in which it should have arrived at Napier, the invoice value will be

accepted. *See, e.g., Terman Foods, Inc. v. Omega Lines*, 707 F.2d 1225, 1228 (11th Cir. 1983); *M. Prusman Ltd. v. M/V Nathanel*, 684 F. Supp. 372, 374 (S.D.N.Y. 1988); *C. Itoh & Co. (America), Inc. v. Hellenic Lines, Ltd.*, 470 F. Supp. 594, 598 (S.D.N.Y. I979).

SALES PROCEEDS ON SALVAGE.

The gross proceeds of the Tampa cargo sold at Antwerp was $2,599,328.00. Undisputed sales expenses of $280,211.00 were incurred on the Tampa cargo, yielding net sales proceeds for the Tampa cargo of $2,319,117.00.

SGS argues that, since, upon discharge at Antwerp, only a small fraction of the cargo was found to be heavily damaged with barley, the cargo should be found not to have lost value except to the extent of that fraction. This argument is unpersuasive. That plaintiff was able to

obtain a good recovery for the cargo at Antwerp does not belie the extreme reduction in value of the cargo at its place of destination, Napier. The good recovery obtained by plaintiff at Antwerp ultimately inures to SGS's benefit by reducing plaintiff's damages.

Defendant, also argues, citing *Trade Arbed, Inc. v. M/V Swallow*, 688 F. Supp. 1095, 1106 (E.D. La. 1988), that when it is possible to segregate sound from damaged cargo, a carrier is liable only for the diminished value of the damaged portion. But it has not been established "that a discrete, identifiable portion of the cargo was not actually damaged." 688 F. Supp. at 1106. Defendant has not established that plaintiff could have achieved a better economic result had it separated the cargo into "heavily damaged" and "said to be sound" lots in Napier.

"Said to be sound" fertilizer apparently was acceptable in Europe, but there is no showing that the New Zealand farmers would have accepted it as uncontaminated. On the contrary, it is clear that they would not. The evidence does not support the conclusion that it would have been economic to discharge, store, clean and then attempt to sell the fertilizer at Napier, much less that it was unreasonable for Interore to have made the choice it made.

EXPENSES OF SALVAGE.

Demurrage.

Interore seeks $93,485.66 in demurrage expense for 58 days in which the ship remained at Napier. For nearly a month after the ship arrived at Napier and the cargo was rejected by East Coast, Interore pursued efforts to have East Coast accept the cargo; when that failed, efforts were

made to salvage it through other buyers. SGS is entitled to a reduction of the sum requested by $24,225.00, an amount already received by Interore from its insurer, Firemen's Fund, for demurrage incurred at Firemen's Fund request so that representatives of Firemen's Fund could inspect the cargo at Napier. That demurrage is not properly chargeable to SGS, and Interore has in any event already been reimbursed for it. That Firemen's Fund is plaintiff's subrogated insurer does not alter this result. No proof was offered that the period of delay attributed to Firemen's Fund in any way contributed to the mitigation effort or is otherwise properly chargeable to SGS.

In addition, since the balance of $69,260.66 ($93,485.66 - $24,225.00) represents demurrage for the entire ship, which was carrying both the Tampa cargo

involved in this litigation and the Swedish cargo, the demurrage should be prorated by weight. The parties have agreed that the Tampa cargo constituted 66.88% of the total. Therefore, the amount of demurrage reasonably attributed to Interore's mitigation efforts is $46,321.53.

Ocean Freight.

Interore seeks to recover ocean freight charges of $575,813.00 plus a $14,764.00 sum described as an "address commission," which Interore retained, for a total of $590,577.00, for transporting the Tampa cargo on the M/V Adelina from Napier to Antwerp. First, Interore is not entitled to the $14,764.00, which it did not in fact pay as freight, but retained. Second, according to the charter party covering the voyage, the freight was calculated on a per ton basis, and the Swedish cargo was

also on board. Therefore, as with the demurrage, Interore's ocean freight expense should be prorated by weight to $385,103.88 ($575,813.00 x 66.88%). So reduced, the ocean freight is properly deducted from the salvage proceeds as necessary to effect plaintiff's mitigation of its damages.

Marine Insurance.

Although Interore did not insure the cargo from Tampa to New Zealand, because it did not consider itself to have title, after East Coast refused to take delivery, Interore insured the Tampa cargo from New Zealand to Antwerp, at a prorated cost of $29,599.67. This expense was reasonably incurred as part of the salvage operation and therefore is properly deducted from the salvage proceeds.

Surveyor Fees.

SGS argues that the surveyor fees were not reasonably related to the salvage operation, but rather were litigation costs. Interore's position is that they were incurred to determine the amount of damage in New Zealand and to record and assist the salvage at Antwerp.

The evidence supports that some, but not all, of Interore's survey expenses were reasonably incurred as part of its effort to mitigate its damages. The following expenses are found to be reasonable:

$1,191.00 to Beckman & Jorgensen

$ 5,521.67 to Dominion Adjusters

$ 53.72 to SGS Van Bree

$1,642.16 to Yves de Grave

$1,631.25 to Dr. Thomas Carroll

The total, $10,039.80, must be prorated by weight (66.88%), which yields $6,714.62.

Warehouse Costs.

Interore paid $83,523.84 for warehousing the Tampa cargo in Antwerp during the salvage operation. This expense was reasonably incurred in order to effectuate mitigation of plaintiff's damages. SGS argues that the sum of $21,487.00, included in that amount, which was a surcharge negotiated by Mr. Etien, should be excluded as unreasonable. Based upon Mr. Etien's testimony, this expense was necessary and reasonable and therefore is fairly charged to SGS as an expense of salvage.

Discharge Costs.

Interore incurred discharge, *i.e.*, stevedoring, costs of $86,551.64 at Antwerp for the Tampa cargo and seeks to reduce its salvage recovery by that sum as a reasonable expense of salvage. SGS argues that, since Interore would have had

discharge expenses at the port of destination, it cannot deduct the discharge expenses incurred in Antwerp. Interore responds that, since its contract with East Coast was "free out," meaning that East Coast and not Interore bore discharge expenses, Interore may properly deduct its discharge expenses from its salvage recovery.

Without regard to whether Interore or East Coast was responsible for discharge at Napier, since Interore's ability to salvage the cargo depended on its discharging the cargo -- and presumably the price it obtained from its buyers reflected the fact that Interore paid for off-loading -- it is reasonable to deduct Interore's discharge expenses from its salvage recovery.

Inland Freight.

It is undisputed that Interore was

invoiced and paid $6,320.98 for inland freight for the Tampa cargo during the salvage of the Tampa cargo. This amount is reasonably deductible from the salvage proceeds.

Miscellaneous Expenses.

It is undisputed that Interore was invoiced and paid $714.63 for bank and miscellaneous expenses relating to the salvage of the Tampa cargo. This amount is reasonably deductible from the salvage proceeds.

CREDITS TO DEFENDANT.

SGS seeks "credit," *i.e.*, a reduction in the damages, for weight loss to the entire Tampa cargo and water damage to the cargo in Hold No. 5, and it seeks to share in a recovery which Interore received in a settlement with East Coast.

Weight Loss.

When the cargo was off-loaded in

Antwerp, it was determined to be short. Defendant argues that it is entitled to a weight loss credit of $39,533.00 reflecting the pro rata value, by weight, of the shortage. Plaintiff's sole argument in response is that, since title had passed to East Coast as soon as the cargo was loaded on the ship, East Coast was at risk for the weight loss, not plaintiff; therefore, plaintiff would have been paid the total invoice value, had the cargo not been contaminated.

To begin with, when and how the weight loss occurred is not clear from the record. Plaintiff argues that it occurred of necessity because of the handling involved in the salvage operation, but the evidence does not establish that. In any event, SGS is simply not responsible for weight shortage. While defendant is properly charged with reasonable salvage

expenses, since they reduce plaintiff's salvage recovery, it is not properly charged with damage to the cargo not attributable to its conduct. It is one thing to say that Interore can use the invoice value as the starting point for determining fair market value at the point of destination. It is another to say, as Interore in effect does here, that SGS bears the risk of weight loss as if it stands in the shoes of the buyer and is liable on the contract. Thus, the total damages to Interore must be reduced by the weight loss.

Water Damage.

Similarly, $17,829.31 worth of the Tampa fertilizer was found to be water damaged upon arrival at Antwerp. SGS is entitled to have the damages reduced by this amount, because it is not responsible for that damage. Interore argues that the

water damage occurred during the salvage operation and therefore is reasonably chargeable to SGS. I disagree. Whether viewed as nonforeseeable, or as caused by an intervening agency, the water damage cannot fairly be attributed to SGS's conduct. Interore's argument that the water damaged fertilizer also contained barley does not save its position, for plaintiff simply assumes, without establishing, that that fertilizer was nonsalvageable had there been no water damage. Interore's witness, Mr. Etien, was unable to state whether, had the fertilizer in Hold No. 5 not been water damaged, any of it could have been salvaged as "said to be sound." According to Etien's Report, there was only a small amount of grain in Hold No. 5 and, in light of the water damage, no attempt was made to segregate that portion of the

water damaged fertilizer which contained it. Under these circumstances, SGS may not be charged with any of the loss of the water damaged cargo in Hold No. 5.

Settlement Credit.

The Settlement Agreement with East Coast arises out of litigation in New Zealand between East Coast, Interore and various insurers of East Coast in which Interore and East Coast asserted claims against the other arising out of the Swedish and Tampa cargos. The Agreement provides that East Coast's underwriter will pay Interore $400,000 "relating to the [Swedish] cargo" and allocates payments of any recoveries the parties to the Agreement may receive from prosecuting claims against other parties. The Settlement Agreement further provides that it releases all signatories as to all claims arising out of the alleged sale,

transportation and salvage of all of the cargo, whether loaded at Tampa or Sweden.

SGS acknowledges that Interore was free to seek recovery from any parties responsible to it and that the potential liability of East Coast does not bar Interore from seeking damages from SGS. However, SGS argues, since Interore received $400,000.00 to settle all of its disputes with East Coast, including its disputes over the Tampa cargo, the allocation in the Settlement Agreement must be viewed as "illusory" and SGS given a credit of $261,360.00, based upon an apportionment by value of the Swedish and Tampa cargos. (It is undisputed that the Tampa cargo represented 65.34% of the total value of the two cargos).

SGS offers no legal authority for looking behind the terms of the Settlement Agreement and no factual basis for

determining that the settlement proceeds should be allocated other than as set forth in the Settlement Agreement. *Cf. Hess Oil Virgin Islands Corp. v. UOP, Inc.*, 861 F.2d 1197, 1208 (10th Cir. 1988) (court "must look to the settlement [agreement] to determine the intent of the settling parties as to what damages and claims are covered").[23] Under these circumstances, SGS's request for a credit based upon the Settlement Agreement should be denied.

CALCULATION OF DAMAGES

Invoice Value	$2,691,003.96
Gross Sales Proceeds	$2,599,328.00
Less Sales Expenses	($ 280,211.00)

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[23] Interore's potential claims against East Coast were not identical to those against SGS, nor were the measures of damages identical. Interore here obtains damages for negligent representation, not breach of contract, and has been awarded only half of those damages in any event.

Net Sales Proceeds		$2,319,117.00
Less Expenses of Salvage Operation		
Demurrage	($	46,321.53)
Ocean Freight	($	385,103.88)
Marine Insurance	($	29,599.67)
Surveyor Fees	($	6,714.62)
Warehouse Costs	($	83,523.84)
Discharge Costs	($	86,551.64)
Inland Freight	($	6,320.98)
Misc. Costs	($	714.63)
Total	($	644,850.79)
Net Proceeds of Mitigation		($1,674,266.21)
Total Damages		$1,016,737.75
Less Damages for Which SGS is Not Responsible, i.e.,		
Weight Loss, $39,533.00		
Water Damage, $17,829.31	($	57,362.31)
Total for Which SGS Shares Responsibility	$	959,375.44
Divided by 2 Yields	$	479,687.72

In sum, plaintiff is entitled to a

damage award against SGS in the amount of $479,687.72.

Prejudgment Interest.

Plaintiff is also entitled to pre-judgment interest on its damages. The parties agree that there is no diversity jurisdiction in this case and that the case therefore arises solely under the court's admiralty jurisdiction. In the absence of special circumstances, which do not exist here, prejudgment interest is recoverable for commercial maritime torts, *E.g., Sutton River Services, Inc. v. Inland Tugs Co., supra*, 1985 A.M.C. at 864. This principle is not affected by plaintiff's shared fault. *See Alkmeon Naviera, S.A. v. M/V "MARINA L"*, 633 F.2d 789, 798 n.12 (9th Cir. 1980). As stated in *Independent Bulk Transport, Inc. v. Vessel "Morania Abaco"*, 676 F. 2d 23, 25 (2d Cir. 1982):

Although it is an abuse of discretion to deny prejudgment interest in admiralty cases except under extraordinary circumstances, *see Mitsui & Co. v. American Export Lines, Inc.*, 636 F.2d 807, 823 (2d Cir. 1981), the district court has broader discretion to determine when interest commences and what rate of interest to apply. *See The Hygrade No. 24 v. The Dynamic*, 233 F.2d 444, 448 (2d Cir. 1956).

Here, neither plaintiff nor defendant has proposed a particular rate. Plaintiff simply ash the Court to exercise its discretion. Since the pre-judgment interest in this case covers a long period of time, during which interest rates varied considerably, the Clerk should be directed to use the interest rates paid each month on 52-week United States treasury bills during the applicable

period, In re Potomac Transport Inc., Nos. 82 Civ. 0805 (JFK), 83 Civ. 4597 (JFK), 1993 WL 17206 (S.D.N.Y. Jan. 19, 1993). *See Independent Bulk Transport, Inc.*, 676 F.2d at 27 ("Plaintiff is entitled to the income which the monetary damages would have earned, and that should be measured by interest on short-term, risk-free obligations."). I recognize that the interest rate I propose is identical to that used in fixing post-judgment interest and that the pre-judgment rate should not necessarily be the same. In this case, however, that rate is the appropriate one to apply. Finally, in the absence of a single date from which damages flowed, a reasonable intermediate date, February 1, 1986, should be used.

Copies of this report are being mailed today to plaintiff's and defendant's counsel who are hereby put on notice that

any objections to this report must be made in conformity with 28 U.S.C. § 636(b)(1) and Rules 72(b), 6(a) and 6(e) of the Federal Rules of Civil Procedure. Thus, a party must serve and file, with a copy to me, specific written objections to the report within ten (10) days after being served with a copy of this report. A party that fails to file timely objections waives the right to further judicial review, including appellate review, of the decision. *Small v. Secretary of HHS*, 892 F.2d 15, 16 (2d Cir. 1989). *See Thomas v. Arn*, 474 U.S. 140, 148-53, 88 L. Ed. 2d 435, 106 S. Ct. 466 (1985); *Wesolek v. Canadair Ltd.*, 838 F.2d 55, 58 (2d Cir. 1988). Any requests for extensions of time to file objections should be made to Judge Tenney.

Respectfully submitted,

NINA GERSHON

Chief Magistrate Judge

Dated: New York, New York
March 31, 1993

5. **ORDER OF THE COURT OF APPEALS DENYING REHEARING, DATED JANUARY 20, 1995**

UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, in the City of New York, on the 20th day of January one thousand nine hundred and ninety-five.

DOCKET NO.: 93-9046

Filed January 20, 1995

INTERNATIONAL ORE & FERTILIZER CORP.,

Plaintiff-Appellee-Cross-Appellant,

v.

SGS CONTROL SERVICES INC.,

Defendant-Appellant-Cross-Appellee.

A Petition for rehearing containing a suggestion that the action be reheard in banc having been filed by Appellant SGS

CONTROL SERVICES INC.

Upon consideration by the panel that decided the appeal, it is ordered that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges of the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

For the Court,
George Lance III, Clerk
By:

_____
Carolyn Clark Campbell
Chief Deputy Clerk

6. **TRANSCRIPT OF ORAL ARGUMENT IN COURT OF APPEALS ON APRIL 24, 1994**

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

----------X

INTERNATIONAL ORE & FERTILIZER CORP.,

PLAINTIFF-APPELEE-CROSS-APPELLANT

-against-

SGS CONTROL SERVICES, INC.,

DEFENDANT-APPELLANT-CROSS APPELEE.

----------X

DATE OF ARGUMENT: April 24, 1994

DATE TRANSCRIBED: March 20, 1995

ORAL ARGUMENT held in the above

matter, at the United States Court of Appeals for the Second District, 40 Foley Square, New
York, New York

DIAMOND REPORTING -718-624-7200- 16 Court St., B'klyn, NY

A P P E A R A N C E S:

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CHARLES B. UPDIKE, ESQ.

* * *

JUDGE A: International Ore & Fertilizer Corp. against SGS Control.

Wait a minute. There should be another ticket, too. There is two appeals.

There should be another one. It is down as two.

VOICE: Consolidated.

JUDGE A: But they've only got--I got to give them much more time than this.

VOICE: According to the calendar--

JUDGE A: According to the calendar, International Ore-- are you for International? You're for SGS.

MR. SCHOEMAN: I'm for SGS, sir.

JUDGE A: And you're on the sanctions point, also?

MR. SCHOEMAN: Mr. Updike will be on the sanctions.

JUDGE A: Well, I want to hear this all together.

MR. SCHOEMAN: Yes, Your Honor.

JUDGE A: So, you have to split 25 minutes between you.

MR. SCHOEMAN: Yes, I understand.

JUDGE A: And the other side gets 20 minutes. We have down here-- and we don't have all the numbers either. Come here for just a second. These two cases are being heard together. This 20/15 and 25. We only have 15 down.

VOICE: 15 minutes for Mr. Schoeman and then ten minutes, that's 25 total.

JUDGE A: Where's the ten?

VOICE: (inaudible).

JUDGE A: I see. Okay. I misunderstood the--good. Thanks. Thanks. Okay. Go ahead.

MR. SCHOEMAN: All right. Your Honor, just so I understand the procedure before we start, will I go first, then Mr. Updike?

JUDGE A: I don't care. You can do it in whatever order you want. It just seems to me that sanctions issue and the merits are intertwined, and I don't know why you're splitting arguments--splitting it up.

MR. SCHOEMAN: That was assigned to us by the clerk's office.

JUDGE A: No. Anybody can make the argument. I mean, I don't care if you--you could have taken the whole time and included the sanctions point.

MR. SCHOEMAN: I understand.

JUDGE A: I mean, the issue of what proximate cause meant and whether the sanctions were appropriately issued, also go to the merits. I just didn't see any point in trying to divide this into a lot-- into an argument of the appeal from the judgment and a separate thing on sanctions, because they are interrelated.

MR. SCHOEMAN: Your Honor, I would like to take 12 minutes and reserve three.

Mr. Updike--

JUDGE A: I'm trying to tell you guys that you got 25 between you.

MR. SCHOEMAN: Yes, sir. Thank you. Your Honor, my name is Michael--

JUDGE A: Now, you're reserving three minutes rebuttal? Okay.

MR. SCHOEMAN: And I believe Mr. Updike will then take eight minutes if he wants to.

JUDGE A: The clock starts running now. They are to stop it after 22 minutes.

MR. SCHOEMAN: Thank you, sir.

JUDGE A: When you give up to Mr. Updike is up to you.

MR. SCHOEMAN: Thank you, sir. This is a maritime case. My name is Michael Schoeman. And I'm here for SGS Control Services.

I think the threshold question in this maritime case is whether the law permits one party to a commercial contract to sue another for negligent misrepresentation in the performance of the contract where the laws is, essentially, economic.

JUDGE A: Well, what if we agreed with that proposition, but agreed with it because we thought the judge was dead wrong in dismissing the contract point?

MR. SCHOEMAN: The contract claim--

JUDGE A: What happens then?

MR. SCHOEMAN: As I understand it, Judge, the contract claim has not been appealed because the briefs for Inter' Ore do not argue the contract point.

JUDGE A: Certainly don't.

MR. SCHOEMAN: So, I think the contract point is foreclosed at this stage in the proceeding.

JUDGE B: But I think now if the case

were to go back to the District Court, it wouldn't be foreclosed, would it?

MR. SCHOEMAN: Well, I would think having abandoned it here, Your Honor, I don't think they could raise it again. They had that choice. It was an easy thing to raise here.

JUDGE B: I understand this. My question is: Because they have not argued on appeal, we're not going to pass on a contract issue now. But assuming, for the argument, that we thought the district judge had made a mistake and we're going to send it back to him, in my opinion, the contract issue will be wide opened again. And I think you should bear that in mind when you're arguing for reversal.

You might get a contract cause of action; instead of getting stuck for 50 percent, you get stuck for 100 percent. I just mention that possibility to you. But

go ahead.

MR. SCHOEMAN: Well, I understand Your Honor. If you send it back, it may be better than where it is now. But I don't think you should send it back on the contract claim, because I think the contract claim is correct. If Your Honor wishes me to address that. But let me first deal with the negligent misrepresentation. But it does flow from the contract. The contract is supposed to provide a proper resolution for a contract dispute between commercial contracting parties. And that seems to be what this Court seems to say in Sundance and other places.

Judge Tenny analyzed the contract claim quite properly. He said, you have a very casual relationship, a phone call followed by a very brief Telex, $150 price. We are not going to assume in that circumstance

that the parties assumed that there could be liability for 2.4 million dollars arising out of that.

JUDGE B: Why not, Counsel?

JUDGE A: Yeah. Why?

MR. SCHOEMAN: Because it is just so disproportionate, Your Honor, to the price that the parties fixed.

JUDGE B: Disproportionate? Your client knew exactly what risk he was taking, did he not?

MR. SCHOEMAN: I don't think so, Your Honor.

JUDGE B: Well, why do they ask to have the hulls inspected and cleaned?

MR. SCHOEMAN: The Certificate of Hull Inspection was a document that was required in a document transaction.

JUDGE B: I understand. But why? Why do they do that?

MR. SCHOEMAN: That--

JUDGE B: To protect, to protect whatever the cargo is going to be; isn't that why they do it? What other reason would there be for having the hulls inspected?

MR. SCHOEMAN: That--

JUDGE B: To protect whatever cargo is going to go in.

MR. SCHOEMAN: That was--

JUDGE B: All right. So, if the cargo is damaged because of a faulty inspection, how can you legitimately argue that that wasn't foreseeable and that it is out of line?

MR. SCHOEMAN: I'm saying that the range of liability was not foreseeable had the parties understood that a two and a half million dollar-- 2.4 million dollar liability claim might arise out of this, it seems to me they would have arranged different terms. I think the court has

dealt with it--

JUDGE A: Are you telling me--

JUDGE B: Well, they should have Counsel. They probably should have. They probably should had more insurance. But that's no reason why you can legitimately argue that the damage was not foreseeable, is it?

MR. SCHOEMAN: Judge, it was-- foreseeability is a peculiar word with different meanings.

JUDGE A: I want to get--

MR. SCHOEMAN: I--

JUDGE A: Is your point that this judgment would have been too high under the contract, but a smaller judgment would have been all right under the contract theory? Is that your theory?

MR. SCHOEMAN: No. My theory is that the parties did not contemplate consequential damage arising out of the

damage to the cargo.

JUDGE A: What if the consequential damages were $300? Judge Tenny's argument that the contract price was too far from the judgment was just far gone out the window.

MR. SCHOEMAN: If the damages-- somewhere there is a line, I agree.

JUDGE A: Well, there's a line. The line is in the, apparently, in your view-- I-- I don't mean to be attacking you as "in your view." You're relying, and Judge Tenny did, on the opinion of this Court that was concurred by one judge. The other two did not concur and it is yet to become the law in this Circuit. But it is-- it goes-- I mean, this argument that you can get consequential damages up to a point, but damn, it goes too far beyond, because the contract price was too small, I just find silly.

MR. SCHOEMAN: Well, Your Honor, this Court referred to that argument unanimously in the Sundance case and seemed to accept it there.

JUDGE A: In dictum.

MR. SCHOEMAN: Well, it was one of the grounds of decision. I don't know if you can call that dictum, Your Honor. But it is not silly.

It is a concept that's embodied in the restatement as well, Restatement of Contracts; where the damages are grossly disproportionate to the price of the contract, there's an assumption that the parties did not intend that liability to follow.

JUDGE B: There might be an assumption, Counsel, but in this case, I think the assumption is unwarranted. I just don't understand how your client can say, I didn't realize, I didn't realize

that this-- that this cargo would be spoiled if there were impurities in the hulls. How could he-- how could he legitimately say it and realize that?

MR. SCHOEMAN: Let me express it differently. The person primarily liable for all of this is the vessel.

JUDGE B: Oh, no. Counsel.

MR. SCHOEMAN: Because it is the vessel--

JUDGE B: The person primarily responsible for this particular action is the inspector who didn't do his job.

JUDGE A: Who didn't inspect.

MR. SCHOEMAN: No, sir. Let me tell you why.

The vessel is responsible for providing a clean hull. That's in the charter. And it was the vessel that had carried the barley and apparently had not cleaned it

all out, and it was the vessel that had painted over the barley, apparently, so nobody could see it.

The vessel, however, was not a party to the action and, consequently, Judge Tenny allocated liability on his tort theory as between the two parties who were there without any consideration to the fact that in these transactions, the remedy of the person who owns the cargo is against the vessel, not against the inspector.

JUDGE B: Had the vessel owner had been sued in this, Counsel, here, he would have brought a Third-Party action against your client and you would be right back where you are now. Because the vessel owner is entitled to rely on your client the same as the shipper, isn't he?

MR. SCHOEMAN: I think it is the other way around, Judge. The vessel owner is the one with the primarily responsibility.

They can't pass that off to us.

JUDGE A: Why? That's why they hired you for.

MR. SCHOEMAN: The vessel owner didn't hire us.

JUDGE A: Well, that's what somebody hired you for.

MR. SCHOEMAN: Inter' Ore hired us. They had a time charter. But the vessel owner was the person at fault here, and it is true, apparently, that there is some questions as to whether we properly performed the inspection. Judge Tenny doesn't decide that issue, as a matter of fact. He doesn't decide whether it was workman-like or whether it was not workman-like.

JUDGE B: You mean to dispute us to whether your client did a good job? You mean that barley flew from in from the sky someplace?

MR. SCHOEMAN: No, Judge. Because an inspection job depends on the nature of a job. Our evidence was that the Customs report was followed. This was the kind of inspection we always did. This is what everybody should expect from such an inspection. If we-- if we had been told the peculiar requirements in New Zealand, that you can't have grain on there, why, we would have done a different inspection.

JUDGE B: You would have done a better job; is that what you're telling us?

MR. SCHOEMAN: Yes. And so is Judge Tenny.

JUDGE B: I think you should have done a better job without all that. That's why you're supposed to do.

MR. SCHOEMAN: Well, we're not supposed to do-- we're not required to do a perfect job. We're supposed to do a $150

job. We're not supposed to do a $10,000 job. We are not supposed to do $100,000 job. We were hired for a $150 job, and that is a lower level of performance.

JUDGE B: $150 job and to do it right; isn't that what you were hired for?

MR. SCHOEMAN: $150 job, right.

JUDGE B: And you were hired to do it right; isn't that right?

MR. SCHOEMAN: We were hired-- yes, we were hired to do--

JUDGE A: Is that 22? How many minutes is that?

VOICE: It is 12 minutes of--

JUDGE B: Go ahead. I've taken a lot of your time.

JUDGE A: I would like to come back, if you don't mind, Mr. Schoeman.

MR. SCHOEMAN: Yes, sir.

JUDGE A: Aside from the principal of the assumption that disproportionate

damages are not to be tolerated, what is the general measure of damages for breach of contract?

MR. SCHOEMAN: The other party is entitled to put in the position he would have been in, had we performed. That-- that stands the general rule. That's something that, of course, is incompletely inconsistent with the tort theory of damages.

JUDGE A: Now, the next question was, can you even measure the damages in the negligent representation claim?

MR. SCHOEMAN: Well, negligent representation language is the foreseeable damages, foreseeable consequences. But I must point out, Your Honor, that one of the cases we cited, McDermott, was reversed by the Supreme Court last week.

So the measure of damages, apparently, in a tort case is even greater, because

there, the Supreme Court was not concerned that the injured Plaintiff might recover more than his actual damages. The concern there was that the Defendants paid their share, and if one Defendant overpays, why, that's just gravy for the Plaintiff.

So, in a tort case, in admiralty, apparently, the measure of damages can, indeed, exceed the amount the Plaintiff has suffered as damages, based of my reading, at least of McDermott.

I would like Mr. Updike to address the sanctions issue, Your Honor.

MR. UPDIKE: If it please the Court, I am Charles Updike and I would like to get to the sanctions issue.

But before I do that, I would like to address Judge Vangreffen's question with respect to why it is that someone is hired to conduct an inspection in this context, and the nature of the contract, and

whether there is a dispute as to whether the job was properly done.

First of all, a principal reason why an inspector is hired to conduct the inspection in this context is because you have two parties here; one is the vessel, the other is the charterer of the vessel. And the vessel wants to be able to say that it is ready to go at a specific time. The charterer of the vessel wants--can then commence loading.

If the vessel is not ready to load, then it is on the vessel's time that it is not ready to load, and the money involved is substantial. If the vessel is ready to load and the charterer is not ready to load, that's the charterer's problem and, again, the money being countered in that context is substantial.

In great measure, the inspector is hired in this situation as a referee

between those two parties. He comes in and he makes an independent judgment. That's what an independent inspector is; he comes in and makes an independent judgment with respect to that issue and he says, as of this time, the ship is ready to go.

JUDGE B: And how does it get ready to go?

MR. UPDIKE: Huh?

JUDGE B: How does it get ready to go?

MR. UPDIKE: It--

JUDGE B: It is ready to go if it can carry the cargo safely?

MR. UPDIKE: Yes, sir. The inspector makes--

JUDGE A: Isn't that right, Counsel?

MR. SCHOEMAN: I'm sorry?

JUDGE B: It is ready to go if it can carry the cargo safely; isn't that right?

MR. UPDIKE: Well, Your Honor--

JUDGE B: If it can't carry the cargo safely, it is not ready to go; isn't that right?

MR. UPDIKE: Well, Your Honor, if it appears in the professional judgment of that inspector that it is clean, dry, and suitable to carry the cargo in question, then he pronounces that it is ready to go. Now, Your Honor, in this instance, with respect to a dispute as to whether the inspection was done properly, the issue here is, was a workman-like job done. That's the standard. It does haven't to be perfect.

JUDGE B: The answer in this instance was no. He took five minutes to inspect the hull?

MR. UPDIKE: No. I don't--

JUDGE B: Isn't their testimony that he did it in five minutes?

MR. UPDIKE: No, there isn't, Your Honor.

JUDGE B: How much time did he take?

MR. UPDIKE: There absolutely is not. The testimony is he did it--

JUDGE B: How much time did he take?

MR. UPDIKE: --in a half hour. The testimony is he did it in a half hour. And let me address, Your Honor, the condition of those hulls and the other aspects of the inspection.

This cargo was dirt. It is phosphate rock. Its fertilizer is going to be put on the ground. It is a cargo that is dug out of the ground. This inspector went in to look at this vessel to see whether it was clean and dry and suitable to carry that kind of a cargo.

JUDGE B: Let me make sure I understand your argument. Your argument that Judge Tenny was wrong when he found

that the inspector did not do his job properly; is that what you're arguing?

MR. UPDIKE: Your Honor, Judge Tenny made absolutely no such finding, no such finding.

JUDGE A: What?

MR. UPDIKE: No such finding.

JUDGE A: He made findings of how much time he spent. How much-- what he thought was the maximum amount of type he spent on the vessel, didn't he?

MR. UPDIKE: I-- I don't recall if he did, Your Honor. I--

JUDGE B: If he made no such finding, where did he come up with the award?

MR. UPDIKE: He came up with the award, Your Honor-- first, Judge Tenny didn't come up with an award. Judge Tenny determined--

JUDGE B: So, just out of the goodness

of his heart he came up with this award?

MR. UPDIKE: Judge Tenny determined that the language of the certificate that was signed by Captain Leward was such that it did not explain that Captain Leward was unable to see the--

JUDGE B: Come on, Counsel. Come on. He decided this case, that your man didn't do a proper job.

MR. UPDIKE: I don't-- I don't think he did, Your Honor.

JUDGE A: He said he spent--

MR. UPDIKE: And he says--

JUDGE A: Excuse me. He made a finding of facts that he spent approximately ten minutes in each hull.

MR. UPDIKE: In each hull. Which is a half an hour.

JUDGE A: But you said he didn't make any findings.

MR. UPDIKE: I said I didn't recall if

he did, Your Honor.

JUDGE A: Oh.

MR. UPDIKE: I think I said that the testimony was that Captain Leward spent a half sure inspecting these hulls. But I go back to the issue here, Your Honor, the question is whether he did a workman-like job. Captain Leward was not the only man to inspect these hulls. There were five different two-legged human beings with eyes that went into the hulls of these vessels; three of them in Sweden and two of them in Tampa. And none of them, not one of them, detected the barley in this vessel, and the reason for it was it had been painted over. These--

JUDGE B: Where did they inspect it; in Tampa or over in-- over-- where they got the original load, London?

MR. UPDIKE: Sweden.

JUDGE B: Sweden, yes. Where did

they--

MR. UPDIKE: There were inspections conducted in both places, Your Honor.

JUDGE B: Let's not count those in. Let's just count the inspection that was made in Tampa. That's the one that's at issue here, isn't it?

MR. UPDIKE: Well, there were, actually, two inspections made in Tampa. One was done by Captain Leward and then, when they started loading one of the hulls, they decided that for balance purposes, they should stop and transfer that cargo into another hull. When that occurred, the first hull was cleaned out, the cargo was transferred, and an entirely different inspector other than Captain Leward went down into that hull, inspected that hull, and said it was clean, dry and ready to receive a cargo of fertilizer.

JUDGE B: Counsel, let me suggest this to you. There is some interesting questions in this case. Obviously there are. But one of them is not whether your man did a good job.

MR. UPDIKE: Fine.

JUDGE B: That was decided against you. It is a question of fact and why are you here arguing it?

MR. UPDIKE: Well, with respect, Your Honor, I don't believe that Judge Tenny did decide against us.

JUDGE B: It is all right. It is your five minutes. You do what you want, but--

MR. UPDIKE: Well, let me turn, Your Honor, to the issue.

JUDGE A: No. I think not. You just used all your time. You gentlemen have used 25 minutes and didn't get to the sanctions issue, just as I anticipated was going happen when two people try to split

an argument like this. Your time is up.

MR. UPDIKE: I apologize, Your Honor.

JUDGE A: I mean, it was your decision to go to a different issue when you stood up.

MR. SOMMER: If it please the Court, I am Richard Sommer and represent International Ore Fertilizer in this action. I would like to address what was said just a few minutes ago about the settlement agreement and citing McDermott.

The Supreme Court of the United States decided the McDermott case, which is in both briefs, on April 20, 1994. That was last week. And I have a Lexis copy of it. It is the only thing out now. Just got the 1994 Lexis citation 3122.

JUDGE A: The Court is aware of it.

MR. SOMMER: Sir?

JUDGE A: The court is aware of the decision.

MR. SOMMER: Thank you.

Just to pursue on the settlement, of course, the settlement is absolutely divisible. The Swedish cargo was not tried here. It was a separate case. We settled with East Coast. East Coast and Inter' Ore were at each other's throat in New Zealand and decided SGS caused the damage.

And they said, "Well, what are we going to do? Are we going to pursue SGS in Tampa?" We couldn't pursue in Sweden because of-- Counsel told us there were torts and other reasons we couldn't pursue in Sweden. The damage to the Swedish cargo is 800,000, so it was split between East Coast and Inter' Ore, 400,000.

But that settlement was straight up forward and had only to do with the Swedish cargo, and it cannot go to the benefit of SGS in this case. I think

that the Court below, decided this under New York law. The--

JUDGE A: May I interrupt? I'm sorry.

MR. SOMMER: Sir.

JUDGE A: I'm sorry, Mr. Sommer. Did the lawyers agree that New York law apply?

MR. SOMMER: Did we make a stipulation or agreement? No, sir. We just assumed New York law would apply.

JUDGE C: Is there a difference between general maritime law and New York law on the question of negligent representation?

MR. SOMMER: I think not.

JUDGE C: Well, that doesn't matter.

MR. SOMMER: I think not, clearly. And the point I want to emphasize is that under New York law, there clearly is a recovery for negligent misrepresentation. And in their reply brief, SGS suggests that this isn't so. It is only available to third parties. But Glance B. Sheppard

is the Semanal case, George Cardoza case (phonetics), I'm sure you're all familiar with that.

And subsequently, they cite cases saying that only third-parties in New York can pursue under negligent misrepresentation and the cases were decided wrongly.

The Court of Appeals in a-- a year and a half ago, New York Court of Appeals in Prudential against Dewey Valentine, specifically held that you had to have privity. And if you didn't have privity, they went to look for something approaching privity. And, of course, we had privity between SGS and Inter' Ore in this case.

Now, to answer your question, Judge Mitcheler, I think the answer is found in Sundancer, a case-- a maritime case that was before-- that eventually went up to

this Court.

And in Judge Knapp's opinion, he wrote the opinion below, he looked at this very case, the International Ore Fertilizer, SGS case had been decided, the first case, by Judge Tenny. And now we have a maritime law case where they're raising the East River type case as-- which is not at all relevant here.

And this is what Judge Knapp says:

"The facts before us present a sharp contrast to those in International Ore Fertilizer vs. SGS, upon which Plaintiff relies. In that case, rather than having asked the Defendant for a certificate or license that would have permitted the operation of the ship or the obtaining of insurance, the ship owner had asked the Defendant to make an examination of the ship's hull for the specific purpose of determining whether or not there was

sufficient cargo."

Then he describes it as a "sloppy inspection." But then he says this:

"Not surprisingly, Plaintiff was allowed to recover on his claim of negligent misrepresentation."

There are numerous cases where negligent misrepresentation is recoverable as a tort under maritime law.

JUDGE B: I got one more question and I will try to sit by and listen to you. On whose representation did Plaintiff rely?

MR. SOMMER: SGS.

JUDGE B: But Leward was the one who made the representation.

MR. SOMMER: But he's the SGS employee and inspector, he undertook to do it.

JUDGE B: He was an independent contractor.

MR. SOMMER: No. We asked SGS. What SGS does, it is SGS's responsibility. And

it was the SGS certificate that we relied on. The SGS certificate that vessel was clean and ready triggered the loading. I mean, the SGS representative turns to the Chief Officer and says, "Your hull is in very good shape." That's in the record.

JUDGE B: That's Leward's representation.

MR. SOMMER: It is the SGS certificate that was the representation.

JUDGE B: The SGS certificate was not issued until after the vessel had left; right?

MR. SOMMER: The SGS certificate was issued onboard the vessel at 2:15 in the morning signed right in presence of the Chief Officer.

JUDGE B: What certificate was issued?

MR. SOMMER: The Certificate of Cleanliness.

JUDGE B: After the vessel had left?

MR. SOMMER: Before she sailed. Before she loaded. He signed it in the cabinet. It is a finding of fact of-- one of the 46 findings of fact of Judge Tenny.

JUDGE B: There is no indication as to when SGS got it?

MR. SOMMER: Well, Leward's gave it to SGS later on. But its effectiveness was right onboard the vessel. He came onboard at 1:45, looked in the hulls, went to the Chief Officer's cabin, had a cup of coffee. At 2:15 in the morning, he issued SGS a Certificate of Cleanliness. It was there in the cabinet with the Chief Officer. And he told the Chief Officer, "The ship looks pretty good."

JUDGE B: Do you think that--

MR. SOMMER: That triggered-- that triggered-- you cannot load a ship until you get that Certificate of Cleanliness. I don't care if you're loading coal. An

inspector looks around to see if there is rags or lumber or oily cargo. You load orange juice and see that the tank is clean. But once the inspector issues that certificate at 2:15 in the morning, in reliance of that certificate, the vessel was then loaded at four in the morning.

JUDGE B: Do you think it might be a significance to determine whether it was on Leward's statement to the Captain or SGS's issuance of the certificate after the vessel left port that the case may rely on?

MR. SOMMER: Absolutely not. Because--

JUDGE A: Excuse me. Excuse me. Leward-- just to get-- so I understand the question. Leward signed an SGS form at 2:15 in the morning; is that your point?

MR. SOMMER: Yes, sir. Onboard the ship. Doing SGS's job of certifying the

vessel's readiness to load.

It is immaterial when the certificate finally arrived at SGS's office or anyone else's office, because it is also not included among the documents needed for the transaction. It doesn't accompany the invoices or the-- SGS gave a certificate of quantity, they gave a certificate of quality and weight. These are all the documents that move the invoice and the bills of lading and--and not the Certificate of Cleanliness.
That's only to load the vessel.

JUDGE A: Can I ask you why you didn't cross-appeal the dismissal of the contract claim?

MR. SOMMER: Well, one reason, obviously, is I didn't think that we would have Judge Winter and Judge Vangraffer sitting up here. We were concerned--

JUDGE A: Where did you think you were;

the First Circuit?

MR. SOMMER: We were concerned with Sundancer.

JUDGE A: What an answer. What an answer. I mean--

MR. SOMMER: Well, Sundancer and Vital. They gave us Vital. And Judge Tenny's opinion, Judge Tenny said after--

JUDGE A: Vital? Boy, you got two judges-- three-judge panel, and two judges specifically say they don't go along with the point Judge Tenny relied upon.

MR. SOMMER: Well, we got negligent misrepresentation and with take-- we had that one for sure.

JUDGE A: Well, but they appealed it. And their argument now is, you got a-- I mean, they don't say you got a contract claim. But implicit in their argument is that when you've got a contract like this, you don't have a negligent

misrepresentation claim available to you.

MR. SOMMER: But the Court held otherwise, and I think correctly.

JUDGE A: That's why they appealed. I mean--

MR. SOMMER: Well, we certainly-- you put us in a box that we have a contract claim and--

JUDGE A: I didn't put you in the box.

MR. SOMMER: No. No. I'm not saying you. But you understand that we have a chance of recovery. All that Inter' Ore is trying to do is be made whole.

JUDGE A: No. But the District Judge says-- on the one hand, the District Judge says, well, you got what you paid for. It was-- you wanted $150 job, you got $150 job. Then he goes on to say, Ah, but they breached their duty of negligent misrepresentation.

Now, I find his rulings inconsistent.

I can't reconcile them. If you got what you paid for, that's the end of all the claims, as far as I can see.

MR. SOMMER: Yes. But in a contract claim, it may be that I'm limited to what I paid for. I got what I paid for. Although, I don't agree with that argument either. I mean, we had this situation here.

The other side talks about a truck getting a certificate that his brakes are in order and then because of the brakes are negligently maintained, having an accident and suing the guy, gave the certificate that the brakes are in order.

We have a different case here. We have a situation when I get a squeeze into my car and I go to SGS brake repairs and store, pay them 29.90 and get a certificate, and after I roll out of the place, I hit the brakes and I smash my car

'cause they don't work. That's a different, different thing.

JUDGE B: What's different about it?

MR. SOMMER: Because the certificate was issued by the person who actually performed the service.

JUDGE A: The problem is, in this case, as I see it, everybody confuses this with a products liability case. And it is not a products liability case at all. That's where this theory of commercial law and damage to the product involved comes in, and the East River case that the Supreme Court decided. But this is not a East River case, this is not a products liability case. So, I don't know why there is so much talk about East River in this case.

MR. SOMMER: You are absolutely correct, Your Honor. I would just like to

have stopped at the end by saying this case was decided under New York law, under New York law, we have negligent misrepresentation and that's it. And therefore, it should be affirmed.

But the Appellants made so much of East River, I thought I at least had to explain it a way in our brief. It is not a products liability, it is not a manufacturer case-- East River involved these big turbines. It is not a Sundancer case where there was a construction, major reconstruction of a ferry into a cruise ship. It is not an Employees of Wausau case where they was-- where even the designer was engaged in the manufacture of ships.

But they raised the issue saying this prevented us from getting a recovery in negligent misrepresentation. So, we explained away these products liability

and strict liability cases; pointed in our brief to the fact that we are entitled to recover in negligent misrepresentation.

JUDGE A: Mr. Sommer, I would come back to the issue of damages. The Ministry of Agriculture in Australia and New Zealand say, they will admit the fertilizer if you remove the barley, barley seeds. Isn't the measure of damages the cost of removing the barley seeds?

MR. SOMMER: Sir, ministry-- the Ministry of Agriculture said that after the ship sat there for a month and a half. And the surveyor said you could not separate the barley seeds and never were.

Because even if you took a screen mesh, barley and these fertilizer particles are almost the same size. And nobody could-- there was no market for it. If you were a farmer, would you buy this stuff if they told you, Oh, well, we took out the barley

seeds?

You have to understand, this was all over the place. When they opened up the hatch, there were plants growing. This is barley growing all over. And, of course, it was good fertilizer. It is not just dirt. These are monomonium phosphate, dinimonium phosphates (phonetics). These are special blends.

Now, how had-- had the damages-- I think we are confusing two things here. One is foreseeability of damage, which I think is foreseeable that if you contaminate a cargo, that you may have to take it somewhere else. And mitigation.

Now, mitigation means: What can we do to get the best price for the barley? If we had separated out barley seeds in New Zealand, you still could not sold that barley-- you could not sold the fertilizer in New Zealand, couldn't do it. Because

there were rumors that it was tainted with disease and everything else. You couldn't sell it in Southeast Asia. They looked. They tried.

I mean, they had-- they had to pay the murage for this vessel sitting there from August 1st until September 27th. And what they did was they did the best thing they could. They tried-- this is mitigation, not foreseeability; mitigate the damages. They took it to Antwerp.

Because now we're talking about seasons. Don't forget, this stuff is supposed to get there in July or beginning of August for their spring in New Zealand. Now they come back up here in November, they store it in Belgium, where they had a marketing staff, and they never said it was sound. They said it was set to be sound.

And they sold it in small lots over

more than a year to get rid of it. And they got almost the full price, the market value of what they sold it to the New Zealanders. And all they were really recovering was the cost and expenses. And even there, they had to recharter the ship.

I mean, the owner of that vessel, he's sitting there with the fertilizer onboard. He made a good bargain. He said, You either get it off or I'll charge you so much.

So, he-- they took that vessel to Antwerp and Judge Gershon only allowed two-fifths of the freight. Of course, to move that ship was $600,000. But, there again, the Swedish cargo was disallowed. We only got three-fifths, three hulls, of the freight money back.

And separating the barley would have been-- and who knows how much that would

have cost. It certainly wasn't available; you couldn't have used this. But that goes-- we did everything we could to minimize that damage. And we suffered the loss.

JUDGE A: Can you tell me how the case involving a ship that goes from Sweden to Tampa to New Zealand to Belgium involving two Delaware corporations that is before us based on admiralty jurisdiction involves New York law?

MR. SOMMER: Both parties have their principal place of business, both parties-- in New York, both parties cited New York cases and assumed New York law applies. And I think the cases are absence some public policy of both parties, and the Court below applied New York to two New York corporations. I mean, Inter' Ore's office is in Rockefeller Center and SGS's office is in

40-something street.

JUDGE A: There is no maritime law on this subject?

MR. SOMMER: Well, there are very few cases like this on the subject, Your Honor.

JUDGE B: That's for sure.

JUDGE A: Well, this one is not going to straighten anything out.

MR. SOMMER: No.

If I may add, I think we should-- we should just point out that the briefs of our opponents are full of reference to Lloyd certificates and other odds and end which were not found germane below.

JUDGE A: I don't think that is of any relevance to anybody. I don't know what it is. But go ahead.

MR. SOMMER: Well, our position is clearly that, factually, there is nothing clearly erroneous. As far as the

sanctions, I don't think there was any abusive discretion by Senior Judge Tenny. He heard the arguments five times and I respectfully urge that this Court affirm the opinion below in its entirety. Thank you very much.

JUDGE C: Okay.

MR. SCHOEMAN: Your Honor, do we have any time left?

JUDGE A: Yes. You have three minutes.

MR. SCHOEMAN: Thank you, sir.

Your Honor, let me address mitigation. Counsel said they did everything they could to mitigate. They didn't. Because in New Zealand, they were paid. They had the bill of exchange that was what they had bargained for in a document transaction. They handed him their papers and they got the bill of exchange back and they were paid in full. And they should have then collected on the

bill of exchange. A bill of exchange is the equivalent of cash, at least in commercial transactions of this nature. Now, why didn't do that?

JUDGE B: Now, Counsel, do you think businessmen operate or should operate?

MR. SCHOEMAN: Well, that's--

JUDGE B: I got the money, so the hell with you?

MR. SCHOEMAN: No. That's the whole purpose of a document transaction, Your Honor.

JUDGE B: Oh, Counsel, legitimate businessmen don't do that sort of thing.

MR. SCHOEMAN: I'm just saying,Judge, they had a bill of exchange, a valid bill of exchange in their hands and they didn't do anything with it. And opted instead to ship this cargo half way around the world.

Your Honor had made an observation about what Judge Tenny found. I just want

everybody to be clear. Judge Tenny said that the Court need not reach the issue of what workman-like efforts would entail. He did not find that we performed in a workman-like fashion or that we did not. Because he then went on to decide this issue on the disproportionate damage question. The reference is JA543 as to that.

Your Honor, I think the point of this case is that there is a real inconsistency between the tort result and the contract result, and there is no showing by the other side as to why you need to now apply or overlay tort theory over a case that is adequately disposed of on contract claims, on the contract claim basis.

Whether or not one agrees with what Judge Tenny decided on the contract claim basis, it still seems to me that it's a contract case and it ought to be decided

consistently with contract principles.

JUDGE A: Your argument is that even if we think Judge Tenny errored on the contract issue, you still win, because he held in favor of you in the contract issue, against you on the negligent issue, and you're saying that that is a contract case?

(Whereupon, the tape-recording concluded.)

I, MAYLEEN CINTRON, a Notary Public for and within the State of New York, do hereby certify that the above is a correct transcription of my stenographic notes.

_____

MAYLEEN CINTRON

No. 94-1086

Supreme Court, U.S.
FILED
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

SGS CONTROL SERVICES, INC.,

Petitioner,

—v.—

INTERNATIONAL ORE & FERTILIZER CORP.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Was the United States Court of Appeals for the Second Circuit limited in legal theories, or did it have the independent power to apply proper law based on a legal theory that was raised in the complaint, tried and decided by the United States District Court for the Southern District of New York, and specifically addressed in Petitioner's brief to the Court of Appeals?

2. Is there a disproportionality doctrine within the United States Court of Appeals for the Second Circuit, and is there, as Petitioner suggests, an "intra" Circuit dispute within that Court on that disproportionality theory?

STATEMENT REQUIRED BY RULE 29.1

Respondent, International Ore & Fertilizer Corporation ("Interore"), a Delaware corporation, is an indirect, wholly owned subsidiary of Occidental Petroleum Corporation, a Delaware corporation whose shares of common stock are publicly traded on the New York Stock Exchange.

TABLE OF CONTENTS

	PAGE
QUESTIONS PRESENTED FOR REVIEW	i
STATEMENT REQUIRED BY RULE 29.1	ii
TABLE OF AUTHORITIES	iv
OPINIONS BELOW	1
STATEMENT OF THE CASE	2
STATEMENT OF FACTS	5
REASONS FOR DENYING REVIEW ON WRIT OF *CERTIORARI*	7
POINT I WAS THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT LIMITED IN LEGAL THEORIES, OR DID IT HAVE THE INDEPENDENT POWER TO APPLY PROPER LAW BASED ON A LEGAL THEORY THAT WAS RAISED IN THE COMPLAINT, TRIED AND DECIDED BY THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK AND SPECIFICALLY ADDRESSED IN PETITIONER'S BRIEF TO THE COURT OF APPEALS?	8
POINT II IS THERE A DISPROPORTIONALITY DOCTRINE WITHIN THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT, AND IS THERE, AS PETITIONER SUGGESTS, AN "INTRA" CIRCUIT DISPUTE WITHIN THAT COURT ON THAT DISPROPORTIONALITY THEORY?	12
CONCLUSION	14

TABLE OF AUTHORITIES

Cases: PAGE

Hansen v. Director OWCP, 984 F.2d 364 (10th Cir. 1993) 10

International Ore & Fertilizer Corp. v. SGS Control Services, 38 F.3d 1279 (2nd Cir. 1994) 9, 12

International Ore & Fertilizer Corp. v. SGS Control Services, Inc., 743 F.Supp. 250 (S.D.N.Y. 1990) . 4

International Trade AD. v. Rensselaer Polytechnic, 936 F.2d 744 (2nd Cir. 1991) 9

Ithaca Industries Inc. v. C.I.R., 17 F.3d 684 (4th Cir. 1994) 9

Kamen v. Kemper Financial Services, Inc., 500 U.S. 90 (1991) 9

Landsberg v. Scrabble Crossword Game Players, Inc., 802 F.2d 1193 (9th Cir. 1986) 10

National Fed'n of Fed. Employees v. Greenberg, 983 F.2d 286 (D.C. Cir. 1993) 10

Northwest Airlines, Inc. v. County of Kent, Mich., ___ U.S. ___, 114 S.Ct. 855 (1994) 10

Retired Chicago Police Ass'n. v. City of Chicago, 7 F.3d 584 (7th Cir. 1993) 10

Sundance Cruises Corp. v. American Bureau of Shipping, 7 F.3d 1077 (2d Cir. 1993), *cert. denied*, ___ U.S. ___, 114 S. Ct. 1399, 128 L.Ed.2d 72 (1994) 12-13

United States National Bank of Oregon v. Independent Insurance Agents America, 113 S.Ct. 2173 (1993) 9

PAGE

United States National Bank of Oregon v. Independent Insurance Agents of America, ___ U.S. ___, 113 S.Ct. 2173 (1993) 9, 10

Vitol Trading, S.A. v. SGS Control Services, 874 F.2d 76 (2d Cir. 1989) 12, 13

Rules:

28 U.S.C., F. R. App. P. Rule 28(a) 11

28 U.S.C., F. R. App. P. Rule 28(b) 11

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ON PETITION FOR A WRIT OF *CERTIORARI* TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION TO THE PETITION FOR A WRIT OF *CERTIORARI*

Respondent, Interore, respectfully requests that this Honorable Court deny the Petition for a Writ of *Certiorari* seeking to review the judgment of the United States Court of Appeals for the Second Circuit.

OPINIONS BELOW

The order of the United States Court of Appeals for the Second Circuit filed January 20, 1995 denying the Petition for a Rehearing with a Suggestion for Hearing *En Banc* is reproduced in Petitioner's Appendix at pages A-183-184. The opinion of the United States Court of Appeals for the Second

Circuit affirming the judgment of the United States District Court for the Southern District of New York in favor of Respondent and affirming the award of sanctions is officially reported at 38 F.3d 1279 and is reproduced in Petitioner's Appendix at pages A-2-49. The opinions of the United States District Court for the Southern District of New York in favor of Respondent are officially reported at 743 F.Supp. 250 and 828 F.Supp. 1098, and are reproduced in Petitioner's Appendix at A-50-98 and A-99-131. Petitioner has also included the unreported opinion of the Southern District of New York of October 23, 1993 which denied Petitioner's motion for a new trial, at A-132-140, and which awarded sanctions against Petitioner's attorneys, at A-137-140.

STATEMENT OF THE CASE

This case involves the liability, under New York law, for an independently made inspection and for failure to properly issue an inspector's "certificate of readiness", with the understanding that such issuance would trigger the loading of a ship—a case in which there are no significant legal issues, constitutional, criminal or other which merit the attention of the Supreme Court.

Interore, an international trader of fertilizers, contracted to sell on a cost-and-freight basis, five different, specially blended fertilizers, to East Coast Fertilizer Company Limited in New Zealand. Interore chartered a five-hold bulk vessel, the M/V ADELINA, to transport two parcels from Sweden and three parcels from Tampa, Florida to New Zealand.

Interore hired SGS to certify the weight and to certify the quality of these goods, and, germane to this action, Interore hired Petitioner SGS, an independent inspector, to inspect the vessel ADELINA's holds, prior to loading, in order to ensure that the holds were clean, dry, fit and suitable to receive the fertilizer cargo bound, for New Zealand. If SGS found the

holds clean, dry, fit and suitable, its inspector was to issue its standard "Certificate of Readiness", with the understanding that such issuance would trigger the loading of the fertilizer.

The District Court determined that SGS negligently misrepresented the condition of the holds by issuing a Certificate of Readiness stating the holds were inspected and found clean and fit when in fact the SGS surveyor had not thoroughly inspected the contaminated holds. It is not disputed that all the holds contained residual grains of barley from a prior cargo.

Interore, relying on the SGS certification, loaded the fertilizer into the ADELINA's holds, and the vessel sailed for New Zealand. On arrival in New Zealand, the Ministry of Food & Agriculture found that the fertilizer was contaminated by the barley grain that SGS failed to discover. The fertilizers were rejected by East Coast because of the grain contamination. Diligent attempts were made by Interore to sell the fertilizers to other buyers in New Zealand, Australia and other neighboring countries; however these markets did not offer a viable return on the possible sale of the cargo. Consequently, after several months, the cargo was transported, still on board the same vessel, to Antwerp, Belgium, where it was salvaged and sold.

Interore filed suit against SGS in the Southern District of New York on September 2, 1987, to recover for damage to both the Swedish and Tampa fertilizers, alleging causes of action in contract, warranty, negligence and negligent misrepresentation. This claim, to recover for its loss of more than $2,000,000, was never changed.

The trial had been bifurcated into liability and damages phases in proceedings before Judge Robert J. Ward. Senior Judge Charles H. Tenney tried all issues with respect to liability in September-October, 1989, and rendered a decision based on New York law, holding both Interore and SGS equally responsible for the damages claimed by Interore.

International Ore & Fertilizer Corp. v. SGS Control Services, Inc., 743 F.Supp. 250 (S.D.N.Y. 1990).

Thereafter, Judge Tenney referred this matter to Chief Magistrate Judge Nina Gershon for determination of the "amount of damages". Magistrate Gershon tried the damage phase of the case in March, 1992, and rendered a Report and Recommendation on March 31, 1993, finding SGS was liable to Interore for $479,687.72 plus interest at the T-bill rate from February 1, 1986 until the date of the judgment.

Judge Tenney affirmed and adopted all of the recommendations in the Report of Magistrate Gershon in an opinion dated August 10, 1993 (828 F.Supp. 1098), and entered an Amended Judgment, including interest, in favor of Interore against SGS in the amount of $713,666.27 on September 15, 1993.

On August 26, 1993, SGS moved for a new trial. On October 28, 1993, Judge Tenney denied SGS's motion and imposed Rule 11 sanctions against SGS's counsel. Thereafter, on November 29, 1993, Judge Tenney entered judgment for Interore's reasonable attorney fees in the amount of $3,570.57. SGS timely appealed to the United States Court of Appeals, Second Circuit. Interore cross-appealed and sought the full amount of damages. The case was argued on April 25, 1994, and decided on October 24, 1994. The Court of Appeals (Winter and Van Graafeiland) affirmed the judgment against SGS and the award of sanctions, with a dissent by the Honorable Jacob Mishler, District Judge, United States District Court for the Eastern District of New York, sitting by designation.

On January 20, 1995, the Court of Appeals, Second Circuit, denied the Petition of SGS for rehearing and the suggestion for rehearing *en banc*, the Petition having been transmitted to the judges of the Court in regular active service and to any other judge that heard the appeal, and *no* such judge requested that a vote be taken on the suggestion for rehearing *en banc*.

STATEMENT OF FACTS

Respondent, Interore, is a trader of fertilizer products, buying and selling in the international marketplace. Petitioner, SGS, is an international surveying company which provides inspection, testing and control services in connection with the movement of bulk cargoes.

In May-June, 1985, Interore bought from suppliers and then sold to a New Zealand buyer 22,202 metric tons of five different, specially blended fertilizers on a cost and freight basis at a price of $4,118,287.

In order to deliver the fertilizers, Interore chartered the vessel M/V ADELINA, a 27,687 deadweight bulk carrier, for the ocean carriage from Landskrona, Sweden (where two blends were loaded) and Tampa, Florida (where the other three blends were loaded) to Napier, New Zealand.

The contract with East Coast required Interore to secure the services of an independent inspection company to (a) determine the weight of the fertilizers, and (b) sample and perform chemical analyses of the fertilizers. That contract also called for an inspection of the cleanliness of the holds of the vessel employed for the ocean carriage, and, before loading could commence, the issuance of a Certificate of Readiness. That Certificate of readiness was not one of the documents required to be presented for payment.

Interore hired SGS to perform all of the control service duties and to perform the hold cleanliness inspection. The request is set forth in a telex dated June 19, 1985 from Interore to SGS, which states in pertinent part:

> Pls act our behalf performing inspection, sampling and analysis. Pls issue flwg docs: 1) cert of hold inspection, confirming vsls holds were clean, dry and suitable.

* * *

> If any questions relative to above pls contact us promptly.

SGS sub-contracted with Mr. Peter Luard in Tampa to perform the hold cleanliness inspection and issue the Certificate of Readiness. Mr. Luard was a former employee of SGS, with many years of experience, and had performed many fertilizer hold inspections in Tampa.

The M/V ADELINA arrived in Tampa on June 30, 1985, and was brought to the pier at approximately 0145 hours on July 2. The SGS surveyor boarded the M/V ADELINA at 0145 hours (in the early morning darkness, when the vessel docked and was boarded by Customs and Immigration officials), and signed the Certificate of Readiness at 0215 hours, on July 2, 1985.

Within that short time, 0145 to 0215 hours, the SGS surveyor allegedly performed the contracted for inspection. Obviously, SGS did not perform, as the holds were contaminated with grain.

The vessel departed Tampa on July 4, and arrived in New Zealand on August 1, 1985. The New Zealand Government authorities examined the fertilizers on board the vessel and found the entire cargo of fertilizers contaminated with barley grains; indeed, there were barley plants growing amongst the fertilizers. On the same day, the buyer rejected delivery of the fertilizers because of the contamination, and on August 3 the buyer abandoned the cargo.

After a month and a half, Interore rechartered the ADELINA, sailed to Antwerp, Belgium and salvaged the cargo. Chief Magistrate Gershon awarded Interore the difference between its contract prices at New Zealand and the resale prices, plus the expenses in connection with the resale, which included the ocean freight. The District Court halved the damages recoverable by Interore on the ground that

Interore should have warned SGS of the strict import standard of the New Zealand authorities.

The claim of Interore throughout these proceedings has been to recover these losses from SGS, and its cross-appeal was to recover the full amount of the loss. In its complaint Interore sued in contract, warranty, negligence and negligent misrepresentation.

REASONS FOR DENYING REVIEW ON WRIT OF *CERTIORARI*

In its preliminary statement Petitioner concedes that this matter does not involve a constitutional provision, treaty, statute, ordinance or regulation.

No suggestion is made by Petitioner, and it is clear, that the decision of the United States Court of Appeals for the Second Circuit is not in conflict with any decision of any other United States Court of Appeals. Petitioner's suggestions, (1) that there was an abuse of discretion by the Second Circuit, and (2) that the disproportionality doctrine merits review, are discussed below. It is respectfully submitted that Petitioner's request for review is without merit.

POINT I

WAS THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT LIMITED IN LEGAL THEORIES, OR DID IT HAVE THE INDEPENDENT POWER TO APPLY PROPER LAW BASED ON A LEGAL THEORY THAT WAS RAISED IN THE COMPLAINT, TRIED AND DECIDED BY THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK AND SPECIFICALLY ADDRESSED IN PETITIONER'S BRIEF TO THE COURT OF APPEALS?

Petitioner has apparently raised a question whether the United States Court of Appeals for the Second Circuit has abused its discretion for claims that have been "waived", to follow Petitioner's categorization. Petitioner's question ignores the fact that claims of Respondent, Interore, were never waived or changed. From the start, Respondent's suit against SGS was the pursuance of an honest and actual, antagonistic assertion of right. Respondent, Interore, did in fact cross-appeal, seeking the full amount of its damages and not the amount limited by the United States District Court for the Southern District of New York. At no time did Interore make a formal waiver, as suggested by Petitioner.

The Respondent, Appellee below, need not have filed any brief in response to the appeal, and, having availed itself of the opportunity to file a brief, was entitled to advance all or some of its arguments. Indeed, even a cross-appeal is unnecessary when the prevailing party advances arguments that merely provide another avenue to reach a proper conclusion. The District Court's decision dealt with the contract issue under New York law. This Honorable Court has said that an appellate court is not limited to the particular legal theories advanced by the parties, but rather retains the independent power to identify and apply the proper construction of gov-

erning law. *Kamen v. Kemper Financial Services, Inc.*, 500 U.S. 90 (1991). Indeed, Petitioner in its brief states:

> The Court has recognized that a court may consider an issue antecedent to and ultimately dispositive of the dispute before it, even an issue the parties fail to identify and brief in that court. *United States National Bank of Oregon v. Independent Insurance Agents of America*, 113 S.Ct. 2173, 2178 (1993).

Respondent Interore agrees.

A review by this Court is not needed to clarify whether an Appeals Court can reverse, or as in this case affirm, a lower Court's judgment based on a tort theory and substitute a judgment based on a contract theory, asserted below, even though Appellee did not file a cross-appeal on the contract theory only.

The Second Circuit below found that ". . . we may uphold the validity of a judgment on any grounds, whether or not a cross-appeal has been filed. We may not, however, enlarge a recovery absent such a cross-appeal. We therefore affirm [based on a contract theory as opposed to a tort theory]." *International Ore & Fertilizer Corp. v. SGS Control Services*, 38 F.3d at 1283-1284. *See, also, id.* at 1285-6 for discussion of the above holding.

The above holding and subsequent discussion accurately set forth the appellate standard in the Second Circuit and all other Circuits for affirmation of a District Court decision on grounds not raised by way of cross-appeal. As was stated in *International Trade AD. v. Rensselaer Polytechnic*, 936 F.2d 744, 747 (2nd Cir. 1991), "It is " 'an inveterate and certain' " rule that a party need not cross-appeal in order to assert an alternate ground based on the record to support a district court decree." (Citations omitted.)

The above standard is consistent with that in the other Circuits. *Ithaca Industries Inc. v. C.I.R.*, 17 F.3d 684, 686, F.N.

2 (4th Cir. 1994), ". . . Respondent is free to rely upon any matter appearing in the record in support of the decision below without filing a cross-appeal."; *Retired Chicago Police Ass'n. v. City of Chicago*, 7 F.3d 584, 593, F.N. No. 8 (7th Cir. 1993) "[the prevailing party] may advance, in support of the judgment, all arguments they presented to that court." They need not file a cross-appeal just because the District Judge rejected one of [their] arguments on the way to deciding in [their] favor."; *Hansen v. Director OWCP*, 984 F.2d 364, 367 (10th Cir. 1993), ". . . a cross-appeal is unnecessary when a prevailing party merely advances an argument that would provide another avenue by which an ALJ could reach the same favorable judgment."; *National Fed'n of Fed. Employees v. Greenberg*, 983 F.2d 286, 289 (D.C. Cir. 1993), "Plaintiffs therefore have the advantage of the familiar rule that on appeal the prevailing party may support a judgment in its favor on any grounds urged or decided below" (citations omitted); *Landsberg v. Scrabble Crossword Game Players, Inc.*, 802 F.2d 1193, 1197 (9th Cir. 1986), ". . . failure to file a cross-appeal does not, however, constitute a waiver of the contract claim. The theories were argued in the alternative."

The Supreme Court had repeatedly confirmed this appellate standard in the course of deciding other substantive civil, criminal or constitutional issues. *See, Northwest Airlines, Inc. v. County of Kent, Mich.*, ___ U.S. ___, 114 S.Ct. 855 (1994); *United States National Bank of Oregon v. Independent Insurance Agents of America*, ___ U.S. ___, 113 S.Ct. 2173 (1993).

Disingenuously, Petitioner, at page 10 of its Petition, states that SGS did not have a meaningful opportunity to be heard on the contract issue in the Court of Appeals, because of the "waiver" of that issue. For its own reasons, Petitioner included the transcript of the oral argument, where the issue was raised and discussed; but, more importantly, in its brief in the Court of Appeals, Petitioner devoted its First Point to that issue.

Petitioner's Court of Appeals Brief states:

"ARGUMENT

I. INTERORE'S TORT CLAIM MUST BE DISMISSED BECAUSE *INTERORE'S RELATION WITH SGS IS GOVERNED BY COMMERCIAL CONTRACT.*" (Emphasis added.)

Thus, contrary to what SGS asserts in its Petition here, its first and main point (seven pages) in its brief in the Court of Appeals is devoted to its argument on the very point which it now says it did not have the opportunity to brief. It is misleading to this Court for Petitioner to suggest, throughout its argument, that it was deprived of the opportunity to raise issues when this was its main point in its brief below.

Petitioner incorrectly alleges the lack of an expressed standard in order to circumvent the fact that this commercial case about damaged fertilizer does not raise important legal questions or issues of a constitutional nature, criminal procedure or a conflict between the Circuits.

It is to be noted that Petitioner relies on criminal cases on the suggestion of waiver, and overlooks the fact that it is the *appellant* who is required to present issues that the *appellant* desires to litigate. 28 U.S.C., F. R. App. P. Rule 28(a)—compare 28(b) [appellee] ". . . except that a statement of the issues or of the case need not be made unless the appellee is dissatisfied. . . ." Clearly, there is no merit to Petitioner's first presented question.

POINT II

IS THERE A DISPROPORTIONALITY DOCTRINE WITHIN THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT, AND IS THERE, AS PETITIONER SUGGESTS, AN "INTRA" CIRCUIT DISPUTE WITHIN THAT COURT ON THAT DISPROPORTIONALITY THEORY?

There is no disproportionality doctrine in the law of the United States Court of Appeals for the Second Circuit and certainly not in maritime matters. Petitioner raises this theory because it arose in another SGS case with the same counsel, in the *dicta* of one judge. *See, Vitol Trading, S.A. v. SGS Control Services,* 874 F.2d 76 (2d Cir. 1989). The disproportionality theory may be of interest to the Petitioner, but is not a real issue.

There is not any conflict with the holding of the Second Circuit in *Sundance Cruises Corp. v. American Bureau of Shipping,* 7 F.3d 1077 (2nd Cir. 1993), as Petitioner suggests, because, in *Sundance,* the disproportionality doctrine was not reached, since the shipowner in that case did not prevail, and did not provide any evidence that it suffered damages, disproportional or not, from the defendant. Even more important, the Court of Appeals for the Second Circuit does not find an *intra*-Circuit conflict, stating, in *International Ore & Fertilizer Corp. v. SGS Control Services,* 38 F.3d 1279 (2nd Cir. 1994), at page 1285:

> * * * We see no reason whatsoever, therefore, why SGS is not liable for Interore's consequential damages as a result of its breach.
>
> Our recent decision in *Sundance Cruises Corp. v. American Bureau of Shipping,* 7 F.3d 1077 (2d Cir. 1993), *cert. denied,* ___ U.S. ___, 114 S. Ct. 1399, 128 L.Ed.2d

> 72 (1994) *is not to the contrary*. [Emphasis added.] *Sundance* was an action for damages on a contract for the classification for insurance purposes of an ocean-going passenger vessel. The court held that the disparity between the fee charged on the contract and damages sought disclosed that the parties did not foresee the risk of such liability. However, the purpose of the contractual obligation of the ship classification society in *Sundance* contrasts markedly with that of the inspector in *Vitol* and in the present case. *Sundance* likened the suit against the classification society to a case in which "one who causes a vehicle accident . . . then sues the Motor Vehicle Bureau for damages to his car because it issued him a driver's license that falsely represented his fitness to drive." 7 F.3d at 1084. In *Sundance*, the court therefore concluded that "the purpose of the classification certificate is not to guarantee safety, but merely to permit [the ship owner] to take advantage of the insurance rates available to a classed vessel." *Id.* The purpose of the inspection in this case, however, was precisely to guarantee the condition of the hold so as to insure the preservation of the cargo. There is no other reason to perform such an inspection and no other reason to pay for one, whatever the amount.

It should be noted that none of the Judges in regular active service in the Second Circuit requested a vote be taken on the rehearing *en banc*.

Disproportionality is of interest to Petitioner, SGS, because unlike SGS, Sweden, which had a tariff limiting liability, Petitioner SGS had no such tariff. The Court below pointed out that Petitioner could have limited liability in line with the fees charged or SGS, if it did not wish to limit its liability by contract could protect itself with insurance, which apparently it did. The suggestion that there is an intra-Circuit problem on disproportionality is artificial.

CONCLUSION

There is no discrepancy in the present state of the law, nor was there any abuse of discretion, nor is there a reason this Court should set a new standard of discretion for the Courts of Appeals, as there is no such issue in this case.

Respondent respectfully submits, there is no reason for granting a writ of *certiorari*.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

SGS CONTROL SERVICES, INC.,

Petitioner,

—v.—

INTERNATIONAL ORE & FERTILIZER CORP.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITIONER'S REPLY BRIEF IN SUPPORT OF ITS PETITION FOR A WRIT OF CERTIORARI

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TABLE OF CONTENTS

PAGE

TABLE OF CONTENTS i

TABLE OF AUTHORITIES ii

PRELIMINARY STATEMENT 1

POINT 1: THE COURT OF APPEALS ABUSED ITS DISCRETION BY DECIDING THE CONTRACT CLAIM THAT THE TRIAL COURT HAD REJECTED AND THAT INTERORE WAIVED ON THE APPEAL 2

POINT 2: WHETHER THE DISPROPORTIONALITY PRINCIPLE APPLIES IN MARITIME CASES IS A QUESTION THAT MERITS CONSIDERATION BY THE COURT..... 4

CONCLUSION..... 5

TABLE OF AUTHORITIES

Case	PAGE
Sundance Cruises Corp. v. American Bureau of Shipping, 7 F.3d 1077 (2d Cir. 1993), *cert. denied*, 114 S. Ct. 1399 (1994)	4

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PRELIMINARY STATEMENT

Petitioner SGS Control Services, Inc. ("SGS) respectfully submits this Reply Brief in reply to the Brief in Opposition of respondent International Ore & Fertilizer Corp. ("Interore").

POINT 1

THE COURT OF APPEALS ABUSED ITS DISCRETION BY DECIDING THE CONTRACT CLAIM THAT THE TRIAL COURT HAD REJECTED AND THAT INTERORE WAIVED ON THE APPEAL.

Point I of SGS's Petition properly raises the question of the standard under which a court of appeals may sua sponte sustain a judgment on the alternate ground of a claim rejected by trial court and waived by the proponent of the claim.

Notwithstanding the absence of a "formal waiver" (*see* Resp. Br. at 8), there is no doubt that in the court of appeals, Interore waived its contract claims. It failed to identify any contract claim as an issue, it failed to brief any contract issue, and it failed to raise any contract issue as an alternative ground of decision, whether in its brief or at oral argument.

Interore now presents the irrelevant argument (as did the court of appeals majority opinion) that an appellee need not cross-appeal to assert an alternate ground to support a district court decree. Resp. Br. at 9. The argument is irrelevant because Interore never asserted any alternate ground to support the judgment. For tactical reasons (because it evidently thought that tort damages would be greater than contract damages), it deliberately abandoned its contract claims and pursued only its tort claim in the court of appeals.

Notwithstanding the assertions in Respondent's Brief at 8, 10-11, SGS's Petition was neither disingenuous nor misleading about SGS's argument in the court of appeals. SGS's Petition clearly and accurately described the first argument of its initial brief in the Second Circuit. See Pet. at 5 ("SGS's appellant's brief to the court of appeals argued that liability could not be founded in tort because the dispute was governed by contract" [footnote referring to additional arguments omitted]). That argument was in fact adopted by the court of

appeals in rejecting the trial court's finding of liability based on tort.

That argument, whether or not tort law governed, is not what Interore waived or what SGS had no opportunity to brief. See Resp. Br. at 10-11. What Interore waived, and what SGS did not get the chance to brief, were Interore's claims, asserted unsuccessfully in the trial court and abandoned on the appeal, that SGS was liable to Interore for breach of contract.

The trial judge had dismissed the contract claims on the ground that the damages sought were not contemplated by the parties. Consequently the trial judge never decided whether there was a breach. SGS, as the party that prevailed on the contract claims, did not present the contract claims to the court of appeals for review. Interore, as the party adversely affected by dismissal of the contract claims, completely abandoned them, and therefore waived them, in the court of appeals. Since Interore had abandoned the contract claims, it would have been improper for SGS's reply brief to respond to them and SGS did not respond to them.

Moreover, even if, *arguendo*, SGS's initial brief had raised the contract claims, Interore's failure to address them in its brief or at oral argument was still a waiver.

Despite the failure of the District Court to decide whether there had been a breach, despite Interore's abandonment of the contract claims in the court of appeals, despite the lack of opportunity for SGS to address the merits of the contract claims, the court of appeals sua sponte decided that the contract had been breached and that the judgment would therefore be affirmed. That action by the court of appeals (and not its decision that tort law was applicable; see Resp. Br. at 10-11) was the abuse of discretion for which SGS seeks review.

POINT 2

WHETHER THE DISPROPORTIONALITY PRINCIPLE APPLIES IN MARITIME CASES IS A QUESTION THAT MERITS CONSIDERATION BY THE COURT.

Interore contends that the second question presented in SGS's Petition, as to the applicability of the Disproportionality Principle in maritime cases, "is not a real issue" (Resp. Br. at 12). Interore's contention is wrong.

Whether the Disproportionality Principle applies in maritime cases is of great significance for the entire shipping industry. Hundreds of billions of dollars worth of goods are shipped annually to and from the United States by maritime transport. Virtually all of this commercial activity is dependent upon the services of maritime service companies. Much of these services is contracted for on an informal basis. Both the service companies and the shippers and receivers of this enormous maritime trade are affected by whether or not the Disproportionality Principle applies to their informal commercial dealings.

Interore argues that there is no conflict in the Second Circuit because the Disproportionality Principle "was not reached" in *Sundance Cruises Corp. v. American Bureau of Shipping*, 7 F.3d 1077 (2d Cir. 1993), *cert. denied*, 114 S. Ct. 1399 (1994). See Resp. Br. at 12. In fact, the *Sundance* opinion expressly relies upon the Disproportionality Principle. *See* 7 F.3d at 1084. And in the present case, the dissenting panel member argued that *Sundance* required that the contract claim be dismissed because of the disproportion between the damages sought and the price of the informal contract between the parties. App. A-44-49. On the other hand, the majority panel members (without overruling *Sundance*) held that under maritime law the Disproportionality Principle had no application here, regardless of how extreme the disproportion might be. App. A-25-27. The conflict and confusion are very real.

SGS respectfully submits that the importance of the question presented and of the affected industry, and the confusion generated by the Second Circuit opinions, amply warrant consideration by the Court of the question presented.

CONCLUSION

For the foregoing reasons, and those set forth in the Petition, petitioner respectfully prays for issuance of a writ of certiorari to the United States Court of Appeals for the Second Circuit.

Dated: New York, New York
May 22, 1995

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